



# Office of Inspector General

**REPORT OF AUDIT OF THE  
DEPARTMENT OF VETERANS AFFAIRS  
CONSOLIDATED FINANCIAL STATEMENTS  
FOR FISCAL YEARS 2000 AND 1999**

**REPORT NO. 00-01702-50**

**DATE: February 28, 2001**

**Office of Inspector General**  
Washington DC 20420



**DEPARTMENT OF VETERANS AFFAIRS**  
**Office of Inspector General**  
**Washington DC 20420**


**Memorandum to the Acting Assistant Secretary**  
**For Management (004)**  
**Report of Audit of the Department of Veterans Affairs Consolidated**  
**Financial Statements for Fiscal Years 2000 and 1999**

1. Attached is the Office of Inspector General's (OIG) Report of Audit of the Department of Veterans Affairs (VA) Consolidated Financial Statements (CFS) for Fiscal Years (FY) 2000 and 1999. The audit was made pursuant to the Chief Financial Officers (CFO) Act of 1990. The OIG contracted with the independent public accounting firm Deloitte & Touche LLP to perform the audit of VA's FY 2000 CFS. The independent auditors' report by Deloitte & Touche provides an unqualified (i.e., clean) opinion on VA's FY 2000 CFS. The OIG defined the requirements of the audit, approved the audit plans, monitored the audit, and reviewed the draft reports. We agree with the auditors' opinion, and the conclusions in the related report on the Department's internal control over financial reporting and compliance with laws and regulations. The OIG conducted the audit of VA's FY 1999 CFS and provided an unqualified opinion on those financial statements.
2. VA has demonstrated management commitment to addressing material internal control weaknesses previously reported and made significant improvements in financial management in a number of areas. The related report on internal controls and compliance with laws and regulations cites the Department's progress towards improving material weaknesses in information technology security controls, Treasury reconciliations, and Housing Credit Assistance (HCA) program accounting. However, opportunities exist for further improvement.
3. The report section on internal controls continues to identify information technology security controls as a material weakness and adds integrated financial management system and control issues as a new material weakness. The report also discusses three other reportable conditions that, while not considered material weaknesses, are significant system or control weaknesses that could adversely affect the recording and reporting of the Department's financial information. These reportable conditions address the need for improving application programming and operating system change controls, business continuity and disaster recovery planning, and operational oversight.
4. The report section on compliance with laws and regulations also concludes that the issues concerning an integrated financial system and information technology security controls contained in the internal control section indicate noncompliance with the requirements of the Office of Management and Budget's (OMB) Circular A-127, "Financial Management Systems", which incorporates by reference OMB Circulars A-123, "Management Accountability and Control", and A-130, "Management of Federal Information Resources." Further, the report concludes that the departures from the OMB requirements are instances of substantial noncompliance with the Federal financial management system requirements of the Federal Financial Management Improvement Act.

5. The material weakness concerning the Department's financial management systems underscores the importance that the Department continue its efforts to acquire and implement a replacement integrated core financial management system. Achieving the success of a clean opinion currently requires a number of "workarounds" involving manual compilations and processes that the financial management system should do. These "workarounds" require extraordinary effort by Department program and financial management staff and the auditors. The risk of materially misstating financial information is high with the existing financial reporting systems and the reliance on "workarounds".

6. Additionally, we believe that consideration should be given to centralizing responsibility for financial management within the Office of the Assistant Secretary for Management (Chief Financial Officer). Sustaining the improvements in financial management demonstrated over the past 2 years may be very difficult because of the increasing strain on the human resources that do the work. Financial management staff are stretched thin throughout the organization and this situation is likely to increase in future years when many experienced financial management employees retire. We suggest that the Department's plan for addressing human capital issues include an objective to streamline financial operations under the Assistant Secretary for Management by accelerating the consolidation of financial management functions and facilities. Financial management activities have been or are being consolidated at a number of Veterans Health Administration medical facilities and several Veterans Benefits Administration activities. However, the progress has been slow and needs to be accelerated. The Department's project to acquire and implement a replacement core financial management system provides a window of opportunity for reengineering and streamlining financial operations. Consolidation of financial management responsibility under the Assistant Secretary for Management would assure visibility over staffing needs, improve consistency of financial management systems, provide uniform leadership, and centralize responsibility for financial management.

7. We will follow up on these issues and evaluate implementation actions during the audit of the Department's FY 2001 Consolidated Financial Statements.



**MICHAEL SLACHTA, JR**  
**Assistant Inspector General**  
**for Auditing**

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## **INDEPENDENT AUDITORS' REPORT**

To the Secretary  
Department of Veterans Affairs

We have audited the accompanying consolidated balance sheet of the Department of Veterans Affairs (VA) as of September 30, 2000, and the related statements of net cost, changes in net position, budgetary resources, and financing for the year then ended, collectively referred to as the financial statements. These financial statements are the responsibility of the management of VA. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of VA for the year ended September 30, 1999 were audited by the VA Office of Inspector General (OIG) whose report, dated March 10, 2000, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States and Office of Management and Budget (OMB) Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of VA as of September 30, 2000, and its net costs, changes in net position, budgetary resources and reconciliation of budgetary obligations to net costs for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The required supplementary information on pages 51 - 59 is not a required part of the consolidated financial statements but is supplementary information required by the OMB Bulletin No. 97-01, *Form and Content of Agency Financial Statements*, as amended. This supplementary information is the responsibility of the VA'S management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

To the Secretary  
Department of Veterans Affairs  
February 2, 2001  
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In accordance with *Government Auditing Standards*, we have also issued our report dated February 2, 2001, on our consideration of VA's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

*Deloitte & Touche LLP*

February 2, 2001



**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE BASED UPON THE AUDIT PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Secretary  
Department of Veterans Affairs

We have audited the consolidated financial statements of the Department of Veterans Affairs (VA), as of and for the year ended September 30, 2000, and have issued our report thereon dated February 2, 2001. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and Office of Management and Budget (OMB) Bulletin No. 01-02. "Audit Requirements for Federal Financial Statements."

**INTERNAL CONTROL OVER FINANCIAL REPORTING**

In planning and performing our audit, we considered VA's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reparable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operations of the internal control over financial reporting that, in our judgment, could adversely affect VA's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses.

Five reportable conditions and three other matters are described in the following paragraphs and include significant departures from certain requirements of OMB Circulars A — 127, "Financial Management Systems," which incorporates by reference Circulars A — 123, "Management Accountability and Control," and A — 130, "Management of Federal Information Resources," among other requirements. We believe that the two reportable conditions identified as "Integrated Financial Management System" and "Information Technology (IT) Security Controls" are also material weaknesses.

## **Integrated Financial Management System — Material Weakness**

As defined in OMB Circular A — 127, “a financial management system encompasses automated and manual processes, procedures, controls, data, hardware, software, and support personnel dedicated to the operation and maintenance of system functions.” Such financial management systems shall be designed to provide for effective and efficient interrelationship between software, hardware, personnel, procedures, controls, and data contained within the systems.

With respect to system requirements in the area of financial reporting, OMB Circular A -127 provides that an agency’s financial management system should generate reliable, timely and consistent information necessary for meeting management’s responsibilities, including the preparation of financial statements. Within OMB Circular A -123, the management control processes necessary to ensure that “reliable and timely information is obtained, maintained, reported and used for decision making” are set forth, including prompt and appropriate recording and classification.

During our audit of VA’s 2000 consolidated financial statements, we noted continuing difficulties related to the preparation, processing and analysis of financial information to support the efficient and effective preparation of the VA’s consolidated financial statements. While significant efforts are made at the component and consolidated levels to assemble, compile and review the necessary financial information for annual financial reporting requirements; in many cases, significant manual work-arounds and “cuff” or cut-of-date feeder systems are still in place as the Department has not yet completed its transition to a fully integrated financial management system.

For example, we noted that general ledgers for some smaller funds are maintained outside the existing core financial management system; unreconciled differences between the general ledger and the Property Management System (PMS) subsidiary ledger existed at the time of a conversion of the property management activity for foreclosures under the Loan Guaranty Program to the VA’s core financial management system: an error in the PMS caused new postings to be recorded at up to four times the appropriate values; and a significant number of adjustments were recorded as part of the year-end closing process, many to record additional activities (both budgetary and proprietary) not reflected in the general ledger prior to the year-end close.

We encourage the Department’s efforts to meet its planned financial reporting improvement objectives. However, given the size and complexity of the VA, as well as the current status of the system development and implementation cycles for planned improvements, it is critical that enhanced control, monitoring and reconciliation processes be in place and functioning appropriately throughout the year to ensure accurate and complete financial reporting. Even though fully automated processes may not yet be in place, supplemental manual processes should be implemented and enforced to meet appropriate control objectives.

The preparation of financial statements more frequently during the year would ensure that supporting analyses and reconciliations are completed and reviewed. While this would be a substantial undertaking, we recommend that the Department adopt the goal of the preparation of monthly financial statements and implement a plan to attain that goal over the next few years. The transition of the closing process from an annual one to more frequently could begin with



semi-annual closes, and then move to quarterly closes as the financial reporting process matures.

### **Information Technology (IT) Security Controls — Material Weakness**

VA's program and financial data Continue to be at risk due to serious problems related to the Departments control and oversight of access to its information systems. These weaknesses placed sensitive information, including financial data and sensitive veteran medical and benefit information, at increased risk of inadvertent or deliberate misuse, fraudulent use, improper disclosure, or destruction, possibly occurring without detection. The VA Office of Inspector General reported this condition in its fiscal year 1997, 1998 and 1999 audit reports and made recommendations for VA to implement a comprehensive security program that would improve these controls. VA has acknowledged these weaknesses and reported IT security controls as a material weakness in its FMPIA report for fiscal years 1998 and 1999. During fiscal years 1999 and 2000, VA proposed and took a number of corrective actions that have/will result in a more effective IT security program. The initiatives are in the process of being implemented and the Department has revised its information security management plan (issued November 20, 2000), which is designed to correct the weaknesses and the plan has compressed the timeframes in which it intends to accomplish such activities.

The management plan includes initiatives that would generally address the key elements of a comprehensive security planning and management program. VA's success in improving information security is dependent on VA executing the plan, including obtaining the level of commitment to it throughout VA and obtaining adequate resources to implement the plan. We recommend that the appropriate resources be applied in order that the planned remedial actions will be accomplished within the identified timeframe.

### **Application Program and Operating System Change Controls**

Our reviews noted weaknesses in the application program change controls and operating system change controls at certain VA data centers and selected VHA medical centers. Weaknesses include: inappropriate access capabilities by application programmers and system support staff to production data; lack of application change procedures; inadequate procedures for testing, approving and migrating system software changes; and inadequate application program change tracking procedures.

We recommend that improved controls over program and operating system changes be instituted, communicated and enforced throughout the data and medical center network.

### **Business Continuity and Disaster Recovery Planning**

Our reviews at certain VA data centers disclosed deficiencies in the design and operation of the business continuity/disaster recovery plans. Specifically, we noted certain disaster recovery plans that were not comprehensive, adequately documented or periodically tested in a timely manner; and tape management procedures that were not adequate.

We recommend that procedures be implemented to ensure that appropriate business continuity/disaster recovery plans are developed, documented and tested to reduce the risk that restoration of business processes and information systems may be delayed or ineffective in the event of an emergency.

### **Operational Oversight**

During the audit, we conducted site visits to selected VA medical centers or stations within the Veterans Integrated Service Network (VISN) to test compliance with identified control and reconciliation processes. We noted a number of instances where application of control and reconciliation processes were not done consistently or completely. In certain instances, existing Department procedures for supervisory review were not applied consistently or on a timely basis. Our observations of ineffective or inefficient processes in the areas of property, plant and equipment, medical accounts receivable and accounts payable during our site visits appeared to be pervasive.

We recommend that procedures for appropriate and timely management reviews and account reconciliations be formalized and implemented to achieve improved internal control over financial reporting. Improved monitoring of existing policies and procedures should be implemented

### **Other Matters**

The Department does not have a mature, effective risk management process with which to evaluate potential loss contingencies for pending medical malpractice claims. Until FY 2000, the recording of the necessary accrual for the loss contingencies was based upon the expected claims payments to be made during the subsequent year. In order to recognize the anticipated full cost of the settlements of medical malpractice claims, an actuarial model was prepared for FY 2000 and an adjustment was made to increase the required loss accrual to approximately \$400 million as of September 30, 2000. The Department should ensure that a formal process is established to develop and maintain the data necessary for appropriate financial reporting on an on-going basis.

The Veterans Health Administration (VHA) had significant aged and invalid accounts payable balances as of September 30, 2000, requiring an adjustment of approximately \$14 million for reporting purposes. The Department should ensure that appropriate validation procedures are in place and enforced at the component level to ensure only accurate and valid financial information is reported.

VA does not have an effective process to accumulate information on the Department's future lease commitments for buildings and equipment. While we understand that there is a significant volume of operating leases maintained at the component or satellite station levels, a process to capture the necessary reporting data regarding outstanding financial commitments should be developed and implemented.

### **Follow-up on Previous Report**

In its report in connection with the Ft 1999 VA financial statements dated March 10, 2000, the Office of Inspector General reported three material weaknesses in the areas of (1) Information Systems Security Controls; (2) Housing Credit Assistance (HOP.) Program Accounting; and (3) Fund Balance with Treasury Reconciliations. As discussed earlier, we believe that material weaknesses continue to exist with respect to items (1) and part of (2). We discussed item (1) in the section entitled "Information Technology (IT) Security Controls." While improvements were made in FY 2000 in the HCA Program accounting, including the conversion of activity to the VA's core financial management system, difficulties were noted during the FY 2000 conversion process as discussed above in the section entitled "Integrated Financial Management System." Improvements were noted during FY 2000 with respect to the Fund Balance with Treasury Reconciliation process and, therefore, the previously reported weakness is considered closed.

### **Performance Measures**

Finally, with respect to the internal control related to performance measures reported in Management's Discussion and Analysis, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions, as required by OMB Bulletin No. 01-02. Our procedures were not designed to provide assurance on internal control over reported performance measures and, accordingly, we do not provide an opinion on such control.

We plan to issue our separate report to you, also dated February 2, 2001, on our additional comments on VA's internal control.

### **COMPLIANCE**

The management of VA is responsible for complying with laws and regulations applicable to the agency. As part of obtaining reasonable assurance about whether VA's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts and certain other laws and regulations specified in OMB Bulletin No. 01-02, including the requirements referred to in the Federal Financial Management Improvement Act (FFMIA) of 1996. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion.

Under FFMIA, we are required to report whether the agency's financial management systems substantially comply with Federal financial management systems requirements, applicable Federal accounting standards, and the U. S. Standard General Ledger at the transaction level. To meet this requirement, we performed tests of compliance using the implementation guidance and evaluative criteria issued by OMB.

The results of our tests disclosed instances of noncompliance that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 01-02, and are described below.

The material weaknesses in internal control over financial reporting discussed above and identified as "Integrated Financial Management System" and "Information Technology (IT) Security Controls" indicate that VA is not in full compliance with the requirements of OMB Circulars A — 123, A — 127, and A - 130. As discussed above, we found weaknesses in (1) the design and operation of internal controls over financial reporting, particularly with effectiveness of the enhanced control, monitoring and reconciliation processes in support of the preparation of the Department's consolidated financial statements, given the status of the transition to a fully integrated financial management system; and (2) the effectiveness of the information technology security controls.

We believe these weaknesses, in the aggregate, result in significant departures from certain of the requirements of OMB Circulars A — 123, A — 127 and A - 130, and are, therefore, instances of substantial noncompliance with the Federal financial management systems requirements under FFMIA.

We plan to issue our separate report to you, also dated February 2, 2001, with our additional comments on immaterial instances of noncompliance with certain provisions of laws, regulations, contracts, and grants.

#### **DISTRIBUTION**

This report is intended solely for the information and use of the management of the Department of Veterans Affairs, the Office of Inspector General for the Department of Veterans Affairs, the Office of Management and Budget, the U. S. General Accounting Office, and the U. S. Congress and is not intended to be and should not be used by anyone other than these specified parties.

*Deloitte & Touche LLP*

February 2, 2001

**Department of  
Veterans Affairs**

**Memorandum**

Date: FEB 28 2001

From: Acting Assistant Secretary for Management (004)

Subj: Report of Audit of VA's Consolidated Financial Statements for Fiscal Years 2000 and 1999

To: Michael Slachta, Jr., Assistant Inspector General for Auditing (52)

We have reviewed the Report of the OIG Audit and are delighted with the overall outcome. Please extend to your staff and the staff of Deloitte & Touche LLP our appreciation for their hard work and cooperation during this year's audit process.

We will share the results of the audit as well as the findings on internal controls over financial reporting and compliance with laws and regulations with senior officials in the Veterans Health Administration, Veterans Benefits Administration, and other VA staff and program managers. We will continue to provide you with updates on the Department's progress implementing our management plan to correct the Information Technology Security Controls material weakness. In addition, we will develop a management plan to correct the new material weakness, Integrated Financial Management System, identified during this year's audit.

Again, thank you for all the work that brought us to another successful conclusion of the audit cycle. Please contact me at 273-5589 if you have any questions.

  
D. Mark Catlett

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# DEPARTMENT OF VETERANS AFFAIRS



## CONSOLIDATED FINANCIAL STATEMENTS

FOR FISCAL YEARS  
2000 AND 1999

# FINANCIAL PRESENTATION



## FINANCIAL PRESENTATION

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**DEPARTMENT OF VETERANS AFFAIRS**  
**CONSOLIDATED BALANCE SHEETS** (DOLLARS IN MILLIONS)  
**AS OF SEPTEMBER 30,**

	2000	1999
<b>ASSET</b>		
<b>INTRAGOVERNMENTAL</b>		
Fund Balance with Treasury (Note 2)	\$ 12,434	\$ 16,198
Investments (Note 4)	14,450	14,572
Accounts Receivable, Net (Note 5)	259	731
Other Assets (Note 6)	93	181
<b>TOTAL INTRAGOVERNMENTAL ASSETS</b>	<b>27,236</b>	<b>31,682</b>
<b>PUBLIC</b>		
Investments (Note 4)	221	239
Accounts Receivable, Net (Note 5)	971	579
Loans Receivable, Net (Note 7)	3,834	4,156
Cash (Note 3)	29	61
Inventories (Note 8)	74	76
General Property, Plant and Equipment (Note 9)	11,564	12,036
Other Assets (Note 6)	27	22
<b>TOTAL ASSETS</b>	<b>\$ 43,956</b>	<b>\$ 48,851</b>
<b>LIABILITIES</b>		
<b>LIABILITIES COVERED BY BUDGETARY RESOURCES</b>		
<b>INTRAGOVERNMENTAL</b>		
Accounts Payable	\$ 37	\$ 30
Debt (Note 10)	1,827	2,540
Other Liabilities (Note 11)	2,450	3,127
<b>TOTAL INTRAGOVERNMENTAL LIABILITIES</b>	<b>4,314</b>	<b>5,697</b>
<b>PUBLIC</b>		
Accounts Payable	474	2,336
Liabilities for Loan Guarantees (Note 7)	5,017	5,808
Insurance Liabilities (Note 14)	12,724	12,852
Other Liabilities (Note 11)	3,885	3,875
<b>TOTAL LIABILITIES COVERED BY BUDGETARY RESOURCES</b>	<b>26,414</b>	<b>30,568</b>
<b>LIABILITIES NOT COVERED BY BUDGETARY RESOURCES</b>		
Federal Employee and Veterans Benefits Liabilities (Note 13)	547,285	484,420
Environmental and Disposal Liabilities (Note 17)	240	199
Insurance Liabilities (Note 14)	531	524
Other Liabilities (Note 11)	1,680	1,300
<b>TOTAL LIABILITIES NOT COVERED BY BUDGETARY RESOURCES</b>	<b>549,736</b>	<b>486,443</b>
<b>TOTAL LIABILITIES</b>	<b>576,150</b>	<b>517,011</b>
<b>NET POSITION</b>		
Unexpended Appropriations (Note 15)	4,132	4,748
Cumulative Results of Operations	(536,326)	(472,908)
<b>TOTAL NET POSITION</b>	<b>(532,194)</b>	<b>(468,160)</b>
<b>TOTAL LIABILITIES AND NET POSITION</b>	<b>\$ 43,956</b>	<b>\$ 48,851</b>

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE STATEMENTS.

**DEPARTMENT OF VETERANS AFFAIRS**  
**CONSOLIDATED STATEMENTS OF NET COST**

(DOLLARS IN MILLIONS)

**YEARS ENDED SEPTEMBER 30,**

2000

1999

**NET PROGRAM COSTS (NOTE 19)**

Medical Care	\$ 19,072	\$ 17,573
Medical Education	782	830
Medical Research	718	650
Compensation	19,584	18,520
Pension	3,161	3,249
Education	1,084	944
Vocational Rehabilitation and Employment	496	509
Loan Guaranty	(423)	1,251
Insurance	100	71
Burial	253	224
<b>NET PROGRAM COSTS BEFORE CHANGES IN VETERANS BENEFITS ACTUARIAL LIABILITIES*</b>	<b>44,827</b>	<b>43,821</b>
Changes in Veterans Benefits Actuarial Liabilities (Note 13)		
Compensation	62,600	(94,127)
Burial	(100)	(822)
<b>SUBTOTAL</b>	<b>62,500</b>	<b>(94,949)</b>
<b>NET NON-VA PROGRAM COSTS</b>	<b>(17)</b>	<b>10</b>
<b>NET COST OF OPERATIONS (NOTE 19)</b>	<b>\$ 107,310</b>	<b>\$ ( 51,118)</b>

\*The 2000 and 1999 changes in Veterans Benefit liabilities were reclassified in order not to distort the program cost being reported in the compensation and burial activities.

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE STATEMENTS.

**DEPARTMENT OF VETERANS AFFAIRS**  
**CONSOLIDATED STATEMENTS OF CHANGES IN NET POSITION**  
(DOLLARS IN MILLIONS)

YEARS ENDED SEPTEMBER 30,

	2000	1999
<b>NET COST OF OPERATIONS</b>	\$ 107,310	\$ (51,118)
<b>Financing Sources (Other than Exchange Revenue)</b>		
Appropriations Used	45,508	44,367
Other Non-Exchange Revenue	18	3
Donations	46	44
Imputed Financing	776	786
Transfers-In	-	32
Transfers-Out	(1,083)	(700)
<b>Subtotal</b>	<u>45,265</u>	<u>44,532</u>
<b>Net Results of Operations</b>	(62,045)	95,650
Increase or Decrease in Unexpended Appropriations and Non Operating Changes	(1,223)	(589)
<b>Change in Net Position</b>	<u>(63,268)</u>	<u>95,061</u>
Net Position-Beginning of Period	(468,160)	(563,164)
Prior Period Adjustments (Note 22)	(263)	3
Cumulative Effect of Changes in Accounting Principles (Note 22)	<u>(503)</u>	<u>(60)</u>
<b>Net Position-End of Period</b>	<u>\$ (532,194)</u>	<u>\$ (468,160)</u>

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE STATEMENTS.

**DEPARTMENT OF VETERANS AFFAIRS  
COMBINED STATEMENTS OF BUDGETARY RESOURCES (NOTE 18)**

(DOLLARS IN MILLIONS)

**YEARS ENDED SEPTEMBER 30,**

**2000**

**1999**

**Budgetary Resources**

Budget Authority	\$ 48,667	\$ 47,609
Unobligated Balance at the Beginning of the Period	21,446	20,034
Net Transfers-Prior Year Balance	(117)	(41)
Spending Authority from Offsetting Collections	10,756	9,488
Adjustments	(2,183)	(1,395)

**Total Budgetary Resources**

**\$ 78,569 \$ 75,695**

**Status of Budgetary Resources**

Obligations Incurred	\$ 57,455	\$ 54,250
Unobligated Balance Available	13,662	15,823
Unobligated Balance Not Yet Available	7,452	5,622

**Total Status of Budgetary Resources**

**\$ 78,569 \$ 75,695**

**Outlays**

Obligations Incurred	\$ 57,455	\$ 54,250
Less Spending Authority from Offsetting Collections and Adjustments	(10,895)	(9,868)

**Subtotal**

**\$ 46,560 \$ 44,382**

Obligated Balance, Net Beginning of Period	7,098	7,335
Adjustments to Obligated Balance	124	-
Less Obligated Balance, Net End of Period	(5,402)	(7,098)

**Total Outlays**

**\$ 48,380 \$ 44,619**

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE STATEMENTS.

**DEPARTMENT OF VETERANS AFFAIRS**  
**COMBINED STATEMENTS OF FINANCING (NOTE 21)**

(DOLLARS IN MILLIONS)

YEARS ENDED SEPTEMBER 30,	2000	1999
<b>OBLIGATIONS AND NON-BUDGETARY RESOURCES</b>		
Obligations Incurred	\$ 57,455	\$ 54,250
Less Spending Authority from Offsetting Collections and Adjustments	(10,895)	(9,868)
Donations Not in the VA's Budget	16	15
Financing Imputed for Cost Subsidies	776	786
Transfers-in (out)	(1,066)	1,099
Exchange Revenue Not in the VA's Budget	(496)	(13)
Non-Exchange Revenue Not in the VA's Budget	15	-
Less Trust Fund Receipts Related to Exchange Revenue in VA's Budget	(1,085)	(1,146)
Other Financing Sources	(573)	(570)
<b>TOTAL OBLIGATIONS AS ADJUSTED AND NON-BUDGETARY RESOURCES</b>	<b>44,147</b>	<b>44,553</b>
<b>RESOURCES THAT DO NOT FUND NET COST OF OPERATIONS</b>		
Change in Amount of Goods, Services and Benefits Ordered But Not Yet Provided	68	474
Change in Unfilled Customer Orders	76	(45)
Costs Capitalized on the Balance Sheet	(4,455)	(4,750)
Financing Sources That Fund Costs of Prior Periods	(1,393)	(95,081)
Collections that Decrease Credit Program Receivables or Increase Credit Liabilities	5,251	260
Other	(691)	1,713
<b>TOTAL RESOURCES THAT DO NOT FUND NET COSTS OF OPERATIONS</b>	<b>(1,144)</b>	<b>(97,429)</b>
<b>COSTS THAT DO NOT REQUIRE RESOURCES</b>		
Depreciation and Amortization	912	906
Bad Debts Related to Uncollectible Non-Credit Reform Receivables	116	118
Revaluation of Assets and Liabilities	-	1
Loss on Disposition of Assets	105	124
Other	349	(150)
<b>TOTAL COSTS THAT DO NOT REQUIRE RESOURCES</b>	<b>1,482</b>	<b>999</b>
<b>FINANCING SOURCES YET TO BE PROVIDED</b>	<b>62,825</b>	<b>759</b>
<b>NET COST OF OPERATIONS</b>	<b>\$ 107,310</b>	<b>\$ ( 51,118)</b>

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE STATEMENTS.

## **NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED SEPTEMBER 30, 2000 AND 1999**

**(DOLLARS IN MILLIONS)**

### **1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

#### **BASIS OF PRESENTATION**

The Department of Veterans Affairs (VA) consolidated financial statements report all activities of VA, which include the Veterans Health Administration (VHA), the Veterans Benefits Administration (VBA), and the National Cemetery Administration (NCA) and Departmental staff organizations. The financial statements are prepared to meet the requirements of the Chief Financial Officers (CFO) Act of 1990 and the Government Management Reform Act (GMRA) of 1994. The financial statements differ from the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records. The statements should be read with the understanding that VA is a component unit of the U.S. Government. VA Fiscal Year (FY) 2000 and FY 1999 financial statements are presented in conformity with the Office of Management and Budget's (OMB) Bulletin No. 97-01, "Form and Content of Agency Financial Statements", as amended.

#### **REPORTING ENTITY**

The mission of VA is to provide medical care, benefits, social support, and lasting memorials to veterans, their dependents, and beneficiaries [(38 U.S.C. Section 301(b) 1997)].

The Department is organized under the Secretary of VA. The Secretary's office includes a Deputy Secretary and has direct lines of authority over the Under Secretary for Health (VHA), the Under Secretary for Benefits (VBA), and the Under Secretary for Memorial Affairs (NCA). Additionally, six Assistant Secretaries, an Inspector General, a General Counsel, and the chairmen of the Board of Contract Appeals and the Board of Veterans' Appeals support the Secretary.

#### **BUDGETS AND BUDGETARY ACCOUNTING**

Budgetary accounting measures appropriation and consumption of budget/spending authority or other budgetary resources and facilitates compliance with legal constraints and controls over the use of Federal funds. Under budgetary reporting principles, budgetary resources are consumed at the time of the purchase. Assets and liabilities, which do not consume budgetary resources, are not reported, and only those liabilities for which valid obligations have been established are considered to consume budgetary resources.

#### **BASIS OF ACCOUNTING**

The accompanying financial statements have been prepared in accordance with the Federal Accounting Standards Advisory Board (FASAB) standards and related concepts. The American Institute of Certified Public Accountants (AICPA) designated FASAB as the accounting standard-setting body for Federal governmental entities. As

a result, accounting principles promulgated by FASAB are considered Generally Accepted Accounting Principles (GAAP) for Federal governmental entities.

### **REVENUES AND OTHER FINANCING SOURCES**

Exchange revenues are recognized when earned to the extent the revenue is payable to VA from other Federal agencies or the public as a result of costs incurred or services performed on their behalf. Revenue is recognized at the point the service is rendered. Imputed financing sources consist of imputed revenue for expenses relating to legal claims paid by Treasury's Judgment Fund and post retirement benefits for VA employees. Non-exchange revenue, e.g., donations, are recognized when received, and related receivables are recognized when measurable and legally collectible, as are refunds and related offsets.

### **ACCOUNTING FOR INTRAGOVERNMENTAL ACTIVITIES**

VA, as a department of the Federal Government, interacts with and is dependent upon the financial activities of the Federal Government as a whole. Therefore, these financial statements do not reflect the results of all financial decisions applicable to VA as though the department was a stand-alone entity.

In order to prepare reliable financial statements, transactions occurring between VA components must be eliminated. All significant intra-entity transactions were eliminated from VA's consolidated financial statements.

### **FUND BALANCE WITH TREASURY**

The U.S. Treasury (Treasury) performs cash management activities for all Federal government agencies. The Fund Balance with Treasury represents the right of VA to draw on the Treasury for allowable expenditures. Trust fund balances consist primarily of amounts related to the Post-Vietnam Educational Assistance Trust Fund, The National Service Life Insurance (NSLI) Fund, The United States Government Life Insurance (USGLI) Fund, The Veterans Special Life Insurance (VSLI) Fund, General Post Fund, and The National Cemetery Gift Fund. The use of these funds is restricted.

### **CASH**

Cash consists of Canteen Service and Loan Guaranty Program amounts held in commercial banks. Treasury processes all other cash receipts and disbursements. Amounts relating to the Loan Guaranty Program represent deposits with trustees for offsets against loan loss claims related to sold loan portfolios.

### **INVESTMENTS**

Investments are reported at cost and are redeemable at any time for their original purchase price. Insurance program investments, which comprise most of VA's investments, are in non-marketable Treasury special bonds and certificates. Interest rates for Treasury special securities are based on average market yields for comparable Treasury issues. Special bonds, which mature during various years through the year 2015, are generally held to maturity unless needed to finance insurance claims and dividends. Other investments from VA programs are in securities issued by Treasury, with the exception of the Loan Guaranty Program investments, which are in trust certificates issued by the American Housing Trust, a private entity not associated with the Government.



Allowances are recorded to reflect estimated losses of principal as a result of the subordinated position in American Housing Trust I through V certificates. The estimated allowance computations are based upon discounted cash flow analysis. Although VA continues to use the income from these subordinate certificates to cover the immediate cash requirements of the Federal guarantee on loans sold under American Housing Trust VI through XI certificates and the Veterans Mortgage Trust program, the income is reimbursed to VA and is not used to pay the amount of the realized losses on guaranteed loan sales.

**ACCOUNTS RECEIVABLE**

Accounts Receivable, Intragovernmental consists of amounts due from other agencies. No allowances for losses are required.

Public Accounts Receivable consists mainly of amounts due from patients and third-party insurers for veterans' health care and amounts due from individuals for compensation, pension, and readjustment benefit overpayments. Based on prior experience, allowances for bad debt losses have been established at approximately 12 percent for medical-related receivables, 49 percent for educational-related receivables, and 76 percent for compensation and pension benefit overpayment-related receivables.

**LOANS RECEIVABLE**

Loans Receivables are recorded as funds are disbursed. For loans obligated prior to October 1, 1991, loan principal and interest receivable amounts are reduced by an allowance for estimated uncollectible amounts. The allowance is estimated based on past experience and an analysis of outstanding balances. For loans obligated after October 1, 1991, an allowance equal to the subsidy costs associated with these loans reduces the loans receivable. This reduction is due to the interest rate differential between the loans and the Treasury borrowing, the estimated delinquencies and defaults, net of recoveries, the offsets from fees, and other estimated cash flows.

**INVENTORIES**

Inventories consist of items such as precious metals held for sale and Canteen Service retail store stock and is valued at cost, utilizing the First In First Out (FIFO) method. VA follows the purchase method of accounting for operating, medical, and pharmaceutical supplies in the hands of end users, which provides that these items be expensed when purchased. VA defines an end user as a VA medical center, regional office, or cemetery.

**PROPERTY, PLANT, AND EQUIPMENT**

The majority of the general property, plant, and equipment is used to provide medical care to veterans and is valued at cost, including transfers from other Federal agencies. Major additions, replacements, and alterations are capitalized whereas routine maintenance is expensed when incurred. Construction costs are capitalized as Construction in Progress until completion, and then transferred to the appropriate property account. Individual items are capitalized if the useful life is two years or more and the unit price is \$25,000 or greater. Buildings are depreciated on a straight-line basis over estimated useful lives of 25 to 40 years. Equipment is also depreciated

straight-line over its useful life, usually 5 to 20 years. There are no restrictions on the use or convertibility of general property, plant, and equipment.

All VA heritage assets are multi-use facilities and are classified as general property, plant, and equipment. Depreciation and amortization expense totaled \$912 and \$906 million in FY 2000 and FY 1999, respectively.

#### **OTHER ASSETS**

Public advance payments are primarily to hospitals and medical schools under house staff contracts, grantees, beneficiaries, and employees on official travel.

Intragovernmental advance payments are primarily to the General Services Administration (GSA) and Government Printing Office (GPO) for supplies, printing, and equipment.

#### **ACCOUNTS PAYABLE**

Accounts Payable, Intragovernmental consist of amounts owed to other Federal agencies. The remaining accounts payable consist of amounts due to the public.

#### **LOAN GUARANTEES**

For direct loan obligations and loan guaranty commitments made after 1991, the resulting direct loans are reported net of an allowance for subsidy costs at present value, and loan guarantee liabilities are reported at present value. The present value of the subsidy costs associated with direct loans and loan guarantees is recognized as a cost in the year the direct or guaranteed loan is disbursed. Pre-1992 direct loans and loan guarantees are reported under the allowance for loss method. The nominal amount of the direct loan is reduced by an allowance for uncollectible amounts, and the liability for loan guarantees is the amount VA estimated will most likely require a future cash outflow to pay defaulted claims. Interest is accrued on VA-owned loans by computing interest on a loan-by-loan basis at the end of the month and recording the amount owed as an accrual.

The guaranteed loan sales liability represents the present value of the estimated cash flows to be paid by VA as a result of the guarantee. VA guarantees that the principal and interest payment due on a loan will be paid by the 15<sup>th</sup> of each month. If the payment is not made, VA allows the loan servicer to receive funds from a cash reserve account for the amount of the deficiency. VA guarantees the loans against losses at foreclosure. Although VA will not buy back the loan, VA will pay off the loan loss and foreclosure expenses.

#### **DEBT**

All Intragovernmental debt is due to Treasury and is primarily related to borrowing by the Loan Guaranty Program. The interest rates ranged from 6.04 to 6.36 percent in FY 2000 and from 4.76 to 5.81 percent in FY 1999. VA's financial activities interact with and are dependent upon those of the Federal Government as a whole.

#### **INSURANCE LIABILITIES**

Actuarial reserve liabilities for VA's insurance programs are based on mortality and interest assumptions at the time of issue. These assumptions vary by fund, type of policy and type of benefit. The interest assumptions ranged from 2.25 to 5.0 percent in FY 2000.

**ANNUAL LEAVE**

The accrued annual leave balance is adjusted at the end of the fiscal year to reflect current pay rates for leave that has been earned but not taken. Sick and other types of non-vested leave are expensed as taken. To the extent appropriations are not available to fund annual leave earned but not taken, funding will be obtained from future financing sources.

**WORKERS' COMPENSATION LIABILITY**

The Federal Employees' Compensation Act (FECA) provides income and medical cost protection to covered Federal civilian employees injured on the job, employees who have incurred a work related occupational disease, and beneficiaries of employees whose deaths are attributable to job-related injuries or occupational diseases. Claims incurred for benefits for VA employees under FECA are administered by the Department of Labor (DOL) and are ultimately paid by VA.

Workers' compensation is comprised of two components: (1) the accrued liability which represents money owed by VA to DOL for claims paid by DOL on behalf of VA through the current fiscal year, and (2) the actuarial liability for approved compensation cases to be paid beyond the current year.

Future workers' compensation estimates are generated from an application of actuarial procedures developed by DOL to estimate the liability for FECA benefits. The liability for future workers' compensation benefits includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases and for potential cases related to injuries incurred but not reported. The liability is determined utilizing historical benefit payment patterns related to a special period to estimate the ultimate payments related to that period.

**PENSION, OTHER RETIREMENT BENEFITS, AND OTHER POST-EMPLOYMENT BENEFITS**

Each employing Federal agency is required to recognize its share of the cost and imputed financing of providing pension and post-retirement health benefits and life insurance to its employees, effective with the fiscal year ended September 30, 1996. Factors used in the calculation of these pensions and post-retirement health and life insurance benefit expenses were provided by the Office of Personnel Management (OPM) to each agency to meet this requirement.

VA's employees are covered under the Civil Service Retirement System (CSRS) and the Federal Employees Retirement System (FERS) to which VA makes contributions according to plan requirements. CSRS and FERS are multi-employer plans. VA does not maintain or report information about the assets of the plans, nor does it report actuarial data for the accumulated plan benefits. The reporting of such amounts is the responsibility of OPM.

**VETERANS BENEFITS LIABILITY**

VA provides compensation benefits to veterans who die or are disabled from military service connected causes as well as their dependents. These benefits are provided in exchange for a veteran's military service. The liability for future compensation payments is reported on VA's balance sheet at the present value of expected future

payments, and is developed on an actuarial basis. Various assumptions in the actuarial model, such as the number of veterans and dependents receiving payments, discount rates, cost of living adjustments and life expectancy, impact the amount of the liability.

### LITIGATION

VA is a party in various administrative proceedings, legal actions, and claims brought against it. In the opinion of VA management and legal counsel, the ultimate resolutions of these proceedings, actions, and claims, will not materially affect the financial position or results of operations.

The preparation of the financial statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and disclosed herein.

## 2. FUND BALANCE WITH TREASURY

### FUND BALANCE WITH TREASURY AS OF SEPTEMBER 30,

	2000	1999
<b>Entity Assets</b>		
Trust Funds	\$ 104	\$ 120
Revolving Funds	7,100	5,929
Appropriated Funds	5,104	8,266
Special Funds	59	51
Other Fund Types	23	17
<b>Total Entity Assets</b>	<b>12,390</b>	<b>14,383</b>
<b>Non-Entity Assets</b>		
Special Funds*	-	1,771
Other Fund Types	44	44
<b>Total Non-Entity Assets</b>	<b>44</b>	<b>1,815</b>
<b>Total Entity and Non-Entity Assets</b>	<b>12,434</b>	<b>16,198</b>
<b>Reconciliation of VA General Ledger Balances with Treasury</b>		
Entity VA General Ledger	12,031	15,801
Reconciled Differences	413	368
Unreconciled Differences	(10)	29
<b>Fund Balance with Treasury</b>	<b>\$ 12,434</b>	<b>\$ 16,198</b>

\*The Fund Balance with Treasury amount recorded as a non-entity special fund balance in FY 99 has been returned to Treasury using a newly established Treasury general fund receipt account. Fund Balance with Treasury amounts related to credit reform subsidy downward reestimates will no longer be retained in VA special funds.

**3. CASH****CASH****AS OF SEPTEMBER 30,**

2000

1999

Canteen Service

\$ 1 \$ 1

Loan Guaranty Program

28 60

**Total Cash**

\$ 29 \$ 61

**4. INVESTMENTS****INVESTMENT SECURITIES****AS OF SEPTEMBER 30,**

2000

1999

**Intragovernmental Securities**

Interest Range

Special Bonds

5.875-11.125%

\$ 14,092 \$ 14,213

Treasury Notes \*

5.375-8.5%

57 51

Treasury Bills

4.73-6.15%

39 36

Subtotal

14,188 14,300

Accrued Interest

262 272

**Total Intragovernmental Securities**

\$ 14,450 \$ 14,572

**Other Securities**

Trust Certificates (Loan Guaranty)

\$ 221 \$ 239

**Total Other Securities**

\$ 221 \$ 239

\*The investment in Treasury Notes includes unamortized premiums of \$.18 million as of September 30, 2000 and 1999. Premiums and discounts are amortized on a straight-line basis over the life of the investments.

**OFFSET FOR LOSSES ON INVESTMENTS****AS OF SEPTEMBER 30,**

2000

1999

Investment in Subordinate Certificates at Time of Sale

\$ 424 \$ 424

Cumulative Reductions

(169) (143)

**Subtotal**

255 281

Allocation of Loss Provision

(34) (42)

**Other Securities**

\$ 221 \$ 239

**5. ACCOUNTS RECEIVABLE, NET****ACCOUNTS RECEIVABLE, NET****AS OF SEPTEMBER 30,**

2000

1999

Intragovernmental Accounts Receivable

\$ 259 \$ 731

Public Accounts Receivable, Gross

2,165 1,096

Allowance for Loss Provision

(1,194) (517)

**Net Public Accounts Receivable**

\$ 971 \$ 579

## 6. OTHER ASSETS

### OTHER ASSETS AS OF SEPTEMBER 30,

		2000		1999
Intragovernmental Advance Payments	\$	93	\$	181
Public Advance Payments	\$	27	\$	22

## 7. LOANS RECEIVABLE, NET AND RELATED DISCLOSURES

Direct loan obligations and loan guarantee commitments made after 1991, and the resulting direct loans or loan guarantees, are governed by the Federal Credit Reform Act of 1990. The Act provides that the present value of the subsidy costs associated with direct loans and loan guarantees be recognized as a cost in the year the direct or guaranteed loan is disbursed. Direct loans are reported net of an allowance for subsidy costs at present value, and loan guarantee liabilities are reported at present value. Pre-1992 direct loans and loan guarantees are reported under the allowance for loss method. The nominal amount of the direct loan is reduced by an allowance for uncollectible amounts, and the liability for loan guarantees is the amount VA estimates will most likely require a future cash outflow to pay defaulted claims.

Interest is accrued on VA-owned loans by computing interest on a loan-by-loan basis at the end of the month and recording the amount owed as an accrual.

The recorded value of loans receivable, net, and the value of assets related to direct loans are not the same as the proceeds that VA would expect to receive from selling its loans. VA operates the following direct loan and loan guaranty programs:

- Vocational Rehabilitation and Employment;
- Education;
- Insurance; and
- Loan Guaranty

Under the Loan Guaranty Program, a loan may be made to an eligible veteran by an approved private sector mortgage lender. VA guarantees payment to the holder of such a loan of a fixed percentage of the loan indebtedness, up to a maximum dollar amount, in the event of default by the veteran borrower. When a delinquency is reported to VA and no realistic alternative to foreclosure is developed by the loan holder or VA supplemental servicing of the loan, VA determines through an economic analysis, whether VA will authorize the holder to convey the property securing the loan (foreclosure) or pay the loan guarantee amount to the holder.

### Loans Receivable

Loans receivable represent the net value of assets related to pre-1992 and post-1991 direct loans acquired, defaulted guaranteed loans, and non-defaulted guaranteed loans. For pre-1992 loans, VA employs the allowance for loss method in which the assets are offset by an allowance for loan losses (estimated uncollectible loans). For post-1991 loans, the assets are offset by an allowance for subsidy costs. An analysis of

loans receivable, loan guarantees, the liability for loan guarantees, and the nature and amounts of the subsidy and administrative costs associated with the direct loans and loan guarantees are provided in the tables that follow:

**TOTAL LOANS RECEIVABLE AND RELATED FORECLOSED PROPERTY, NET  
AS OF SEPTEMBER 30,**

<b>2000</b>	<b>LOANS RECEIVABLE GROSS</b>	<b>INTEREST RECEIVABLE</b>	<b>ALLOWANCE FOR LOAN LOSSES</b>	<b>FORECLOSED PROPERTY</b>	<b>VALUE OF ASSETS RELATED TO LOANS</b>
DIRECT LOANS OBLIGATED PRIOR TO FY 1992 (ALLOWANCE FOR LOSS METHOD)	\$ 141	\$ 22	\$ (55)	\$ -	\$ 108
DIRECT LOANS OBLIGATED AFTER 1991	1,535	38	61	19	1,653
DEFAULTED GUARANTEED LOANS PRE-1992 GUARANTEES	\$214	6	(196)	131	155
DEFAULTED GUARANTEED LOANS POST-1991	-	-	-	983	983
NON-DEFAULTED GUARANTEED LOANS (INSURANCE POLICY)	913	22	-	-	935

**TOTAL LOANS RECEIVABLE AND RELATED FORECLOSED PROPERTY, NET** **\$ 3,834**

**TOTAL LOANS RECEIVABLE AND RELATED FORECLOSED PROPERTY, NET  
AS OF SEPTEMBER 30,**

<b>1999</b>	<b>LOANS RECEIVABLE GROSS</b>	<b>INTEREST RECEIVABLE</b>	<b>ALLOWANCE FOR LOAN LOSSES</b>	<b>FORECLOSED PROPERTY</b>	<b>VALUE OF ASSETS RELATED TO LOANS</b>
DIRECT LOANS OBLIGATED PRIOR TO FY 1992 (ALLOWANCE FOR LOSS METHOD)	\$ 155	\$ 59	\$ (69)	\$ -	\$ 145
DIRECT LOANS OBLIGATED AFTER 1991	1,713	45	(124)	24	1,658
DEFAULTED GUARANTEED LOANS PRE-1992 GUARANTEES	329	-	(299)	211	241
DEFAULTED GUARANTEED LOANS POST-1991 (PRESENT VALUE METHOD)	44	-	-	1,119	1,163
NON-DEFAULTED GUARANTEED LOANS (INSURANCE POLICY)	927	22	-	-	949
<b>Total Loans Receivable and Related Foreclosed Property, Net</b>					<b>\$ 4,156</b>



**FORECLOSED PROPERTY**

Prior to the foreclosure of property secured by a VA loan, VA obtains an independent appraisal of the property. This appraisal is reviewed by VA appraisal staff and VA makes a determination of the fair market value. To determine the net value of the property, VA costs for acquisition, management and disposition of the property, as well as estimated losses on property resale, are subtracted from the estimated fair market value. As of September 30, 2000 and 1999, the estimated number of residential properties in VA's inventory was 13,000 and 12,044, respectively. For FY 2000 and FY 1999, the average holding period from the date properties were conveyed to VA until the properties were sold was estimated to be 9 months and 9.7 months, respectively. The number of properties for which foreclosure proceedings are in process is estimated to be 18,500 and 17,906 as of September 30, 2000 and 1999, respectively.

**GUARANTEED LOANS****AS OF SEPTEMBER 30,**

		2000	1999
Outstanding Principal Guaranteed Loans, Face Value	\$	216,360	\$ 214,000
Amount of Outstanding Principal, Guaranteed		71,764	71,900
<b>Liabilities for Loan Guarantees Post 1991 (Present Value)</b>	<b>\$</b>	<b>5,017</b>	<b>\$ 5,808</b>

**GUARANTY COMMITMENTS**

As of September 30, 2000, VA had outstanding commitments to guarantee loans that will originate in FY 2001. The number and amount of commitments could not be determined, as VA has granted authority to various lenders to originate VA loans that meet established criteria without prior VA approval. Nearly 90 percent of VA's guaranteed loans originate under this authority.

**PROVISION FOR LOSSES ON PRE-1992 LOANS**

One element of the cost of the mortgage loan benefit that VA provides to veterans is the present value of the cost VA will bear as loans already guaranteed default in the future. This cost is reflected in the financial statements as an offset to the value of certain related assets.

The provision for losses on guaranteed loans is based upon historical loan foreclosure results applied to the average loss on defaulted loans. The calculation is also based on the use of the average interest rate of U. S. interest-bearing debt as a discount rate on the assumption that VA's outstanding guaranteed loans will default over a 12-year period. The discount rate used in the calculation was 6.6 and 6.5 percent for FY 2000 and FY 1999, respectively. The components of the provision are as follows:

**PROVISION FOR LOSS****AS OF SEPTEMBER 30,**

		2000	1999
Offsets Against Loans Receivable	\$	55	\$ 53
Offsets Against Foreclosed Property Held for Sale		8	7
Offsets Against Investments		-	42
Reserve for Losses on Guaranteed Loans		-	16
<b>Total Provision for Loss</b>	<b>\$</b>	<b>63</b>	<b>\$ 118</b>



**SUBSIDY EXPENSE FOR POST-1991 DIRECT LOANS**

Pursuant to the Credit Reform Act, all direct loans established and guaranteed loans closed after September 30, 1991, will be subsidized. In FY 1999, VA reestimated the subsidy expense for all loan sale guarantees made between FY 1992 and FY 1998, and estimated the subsidy expense for loan sale guarantees issued in FY 1999. The subsidy expense for direct loans and loan guarantees related to the Loan Guaranty Program is as shown:

**DIRECT LOAN SUBSIDY EXPENSE****FOR THE YEARS ENDED SEPTEMBER 30,**

	2000	1999
Interest Differential	\$ (110)	\$ 3
Defaults*	41	119
Fees**	(1,224)	(81)
Other***	1,333	86
<b>Subtotal</b>	<b>40</b>	<b>127</b>
Interest Modifications Reestimates	(107)	(154)
<b>Total Direct Loans</b>	<b>\$ (67)</b>	<b>\$ (27)</b>

\* Includes approximately \$221,000 and \$123,000 in defaults and other expenses for the Vocational Rehabilitation Program for FY 2000 and 1999 respectively.

\*\* "Fee" expense for direct loans includes estimated down payments and other fees collected when homes are sold with vendee financing.

\*\*\* The "Other" expense for direct loans includes the estimated loss of scheduled principal and interest when vendee loans are sold.

**GUARANTEED LOAN SUBSIDY EXPENSES****FOR THE YEARS ENDED SEPTEMBER 30,**

	2000	1999
Defaults	\$ 1,605	\$ 3,242
Fees*	(359)	(819)
Other**	(1,109)	(2,225)
<b>Subtotal</b>	<b>137</b>	<b>198</b>
Loan Modifications Reestimates	(696)	307
<b>Total Guaranteed Loan Subsidy Expense</b>	<b>\$ (559)</b>	<b>\$ 505</b>

\* The "Fee" expense includes estimated up-front fees collected when the loans are guaranteed and the present value of estimated annual fees from loan assumptions.

\*\* The "Other" expense for guaranteed loans includes estimated recoveries on defaults through the sales of foreclosed properties.

**LOAN SALE-GUARANTEED LOAN SUBSIDY EXPENSE****FOR THE YEARS ENDED SEPTEMBER 30,**

	2000	1999
Defaults	\$ 75	\$ 48
Other	4	4
<b>Subtotal</b>	<b>79</b>	<b>52</b>
Reestimates	(75)	360
<b>Total Loan Sale-Guaranteed Subsidy Expense</b>	<b>\$ 4</b>	<b>\$ 412</b>

**SUBSIDY EXPENSE****FOR THE YEARS ENDED SEPTEMBER 30,**

	2000	1999
Total Direct Loans	\$ (67)	\$ (27)
Total Guaranteed Loans	(559)	505
Total Sale Loans	4	412
<b>Total Subsidy Expense</b>	<b>\$ (622)</b>	<b>\$ 890</b>

**Administrative Expense**

Administrative expense on direct and guaranteed loans for the years ended September 30, 2000 and 1999, was \$157 and \$160 million, respectively.

**Loan Sales**

VA continues to have vendee loan sales to reduce the administrative burden of servicing vendee loans. During the period FY 1992 through FY 2000, the total loans sold amounted to \$11.4 billion. Under the sale of vendee loans, certificates are issued pursuant to the Pooling and Servicing Agreement (the Agreement) among VA, the Master Servicer, and the Trustee. On the closing date of the certificates, VA transfers its entire interest in the related loans to the Trustee for the benefit of the related certificate holders pursuant to the Agreement. Under the Agreement, the Trust will issue certificates backed by mortgage loans and installment contracts. The Trust owns the mortgage loans and other property described in the offering and the Trust makes elections to treat certain of its assets as one or more REMICs for U.S. Federal income tax purposes. The certificates represent interests in the assets of the Trust and are paid from the Trust's assets. The certificates are issued as part of a designated series that may include one or more classes. VA guarantees that the investor will receive full and timely distributions of the principal and interest on the certificates and it is backed by the full faith and credit of the Federal Government.

VA may terminate the Trust causing the early retirement of certificates, by purchasing all of the Trust's assets on any distribution date on or after the distribution date on which the current aggregate principal balance of all principal certificates is less than 1 percent of the original aggregate principal balance of the certificates or if VA determines that the Trust's REMIC status has been lost or that a substantial risk exists that such status will be lost. In the event of termination, the certificate holder will be entitled to receive payment for the full principal balance of the certificates plus any accrued interest and unpaid interest through the related distribution date.

The Agreement requires the mortgage loans to be serviced generally in compliance with Fannie Mae and Freddie Mac standards and consistent with prudent residential mortgage loan servicing standards generally accepted in the servicing industry. The mortgage loans are serviced by Countrywide Home Loans, Inc. (formerly Countrywide Funding Corporation) ("CHL" or "Master Servicer"). The Master Servicer is responsible for the performance of all of the servicing functions under the Agreement. The Master Servicer is entitled to be compensated by receiving (1) a service fee of 0.2075 percent per annum payable monthly and calculated by multiplying the interest payment received by a fraction, the numerator of which is 0.2075 percent and the denominator of which is the mortgage interest rate on such loan; (2) earnings on investment of funds in the certificate account; and (3) all incidental fees and other charges paid by the borrowers and a portion of the liquidation proceeds in connection with the liquidated loans.

VA completed four sales during FY 2000 and two sales during FY 1999 totaling approximately \$1.5 billion and \$1 billion of vendee loans, respectively. The components of the vendee sales are summarized in the tables below:

**LOAN SALES****YEARS ENDED SEPTEMBER 30,**

	2000	1999
Loans Receivable Sold	\$ 1,493	\$ 968
Proceeds From Sale*	1,466	960
<b>Loss (Gain) on Receivables Sold</b>	<b>\$ 27</b>	<b>\$ 8</b>

\*Information presented does not reflect the transaction expenses incurred to sell the loans.

**OUTSTANDING BALANCE OF LOAN SALE GUARANTEES**

All loans sold under the American Housing Trust (AHT VI through AHT XI) and the Vendee Mortgage (VMT 92-1 through 00-3) programs carry a full government guarantee. The outstanding balance for guaranteed loans sold is summarized in the table below:

**GUARANTEED LOANS SOLD****AS OF SEPTEMBER 30,**

	2000	1999
Outstanding Balance Guaranteed Loans Sold, Start of Year	\$ 7,610	\$ 6,946
Guaranteed Loans Sold to the Public	1,493	968
Payments, Repayments, and Terminations	(949)	(304)
<b>Outstanding Balance Guaranteed Loans Sold, End of Year</b>	<b>\$ 8,154</b>	<b>\$ 7,610</b>

**LIABILITY FOR LOAN SALE GUARANTEES (POST-1991)**

Starting in FY 1999, VA began reporting the liability on the guarantee of loans sold under the Vendee Mortgage Trust and American Housing Trust programs. All guaranteed loan sales after September 30, 1991, are subject to Credit Reform requirements. For these loans, the guaranteed loan sale liability represents the present value of the estimated net cash flows to be paid by VA as a result of the guarantee. VA guarantees that the principal and interest payment due on a loan will be paid by the 15th of each month. If the payment is not made, VA allows the loan servicer to receive funds from a cash reserve account for the amount in deficiency. VA also guarantees the loan against loss at foreclosure. Although VA will not buy back the loan, VA will pay off the loan loss and foreclosure expenses. The liability for loan sale guarantees is currently \$215 million.

**8. INVENTORIES****INVENTORIES****AS OF SEPTEMBER 30,**

	2000	1999
Held for Current Sale	\$ 60	\$ 65
Excess, Obsolete and Unserviceable	14	10
Held for Repair and Parts	-	1
<b>Total Inventories</b>	<b>\$ 74</b>	<b>\$ 76</b>

## 9. GENERAL PROPERTY, PLANT, AND EQUIPMENT

### GENERAL PROPERTY, PLANT, AND EQUIPMENT AS OF SEPTEMBER 30,

			2000	1999
	Cost	Accumulated Depreciation	Net Book Value	
Land and Improvements	\$ 191	\$ (2)	\$ 189	\$ 176
Buildings	13,824	(5,609)	8,215	7,987
Equipment	3,682	(2,019)	1,663	2,194
Other	1,734	(925)	809	768
Construction in Progress	688	-	688	911
<b>Total Property, Plant, and Equipment</b>	<b>\$ 20,119</b>	<b>\$ (8,555)</b>	<b>\$ 11,564</b>	<b>\$ 12,036</b>

## 10. DEBT

All Intragovernmental debt is due to the Treasury and is primarily related to borrowing by the Loan Guaranty Program. The interest rates ranged from 6.04 to 6.36 percent in FY 2000 and from 4.76 to 5.81 percent in FY 1999. VA's financial activities interact with and are dependent upon those of the Federal Government as a whole.

Intragovernmental debt as of September 30, 2000, and 1999 was \$1,827 and \$2,540 million, respectively. The debt for fiscal year 2000 includes accrued interest payable of \$9.8 million.

## 11. OTHER LIABILITIES

### INTRAGOVERNMENTAL FUNDED LIABILITIES AS OF SEPTEMBER 30,

	2000	1999
Deposit and Clearing Account Liabilities	\$ 12	\$ 15
Accrued Payables - Federal	14	-
Deferred Revenue	84	19
Resources Payable to Treasury	812	731
Custodial Liabilities*	1,420	2,251
General Fund Receipts Liability	22	31
Accrued VA Contributions for Employee Benefits	86	80
<b>Total Intragovernmental Funded Liabilities</b>	<b>\$ 2,450</b>	<b>\$ 3,127</b>

\* The Custodial Liabilities Accounts include subsidy reestimates for loans made after September 30, 1991, which are subject to the provisions of the Credit Reform Act of 1990. The liability provision for future losses on credit reform guaranteed loans is comprised of a funded subsidy for each loan guaranteed at the rate equal to the amount of the present value of estimated loss to the Government for the cohorts of loans. The subsidy amount for each cohort is reestimated annually to ensure amounts reflect the actual losses on guaranteed loans. Based on the reestimated amounts, additional subsidy funds are provided for or excess funds are returned.

**PUBLIC FUNDED LIABILITIES****AS OF SEPTEMBER 30,**

	2000	1999
Accrued Funded Annual Leave	\$ 9	\$ 9
Accrued Payables	1,390	1,205
Accrued Salaries and Benefits	400	558
Contract Holdbacks	21	22
Unredeemed Coupons	1	1
Deposit and Clearing Account Liability	53	45
Unearned Premiums	136	143
Insurance Dividends Left on Deposit and Related Interest Payable*	1,526	1,461
Capital Lease Liability	27	24
Dividend Payable to Policyholders	322	345
Custodial Liability	-	46
Reserve for Losses on Guaranteed Loans	-	16
<b>Total Public Funded Liabilities</b>	<b>\$ 3,885</b>	<b>\$ 3,875</b>

\*Interest earned on dividends left on deposit is paid annually to insurance policyholders on the policy anniversary dates.

**PUBLIC UNFUNDED LIABILITIES****AS OF SEPTEMBER 30,**

	2000	1999
Annual Leave*	\$ 936	\$ 904
Capital Lease Liability	8	1
Judgment Fund-Unfunded**	415	82
Accrued FECA Liability	321	313
<b>Total Intragovernmental Funded Liabilities</b>	<b>\$ 1,680</b>	<b>\$ 1,300</b>

\*Annual leave is accrued when earned and is adjusted at the end of the fiscal year to reflect current pay rates of cumulative leave earned but not taken. Sick and other types of leave are expensed as taken.

\*\* The Judgment Fund liability amount represents the estimate for future payments on legal cases that will be paid by the Treasury Judgment Fund on behalf of VA.

**12. LEASES**

VA has both capital and operating leases. The capital lease liability is \$35 and \$24 million as of September 30, 2000 and 1999, respectively. Due to the number of operating leases and the decentralization of records, the future commitment for operating leases is not known. VA's FY 2000 operating lease costs were \$186 million for real property rentals and \$51 million for equipment rentals. The FY 1999 operating lease costs consisted of \$185 million for real property rentals and \$46 million for equipment rental. The following chart represents VA's estimate for operating lease costs for the next five years, assuming a 3.5 percent yearly increase in cost.

**LEASES:**

YEAR	REAL PROPERTY	EQUIPMENT
2001	\$ 193	\$ 53
2002	200	55
2003	207	57
2004	214	59
2005	221	61

**13. FEDERAL EMPLOYEE AND VETERANS BENEFITS****FEDERAL EMPLOYEE BENEFITS****IMPUTED EXPENSES-EMPLOYEE BENEFITS  
YEARS ENDED SEPTEMBER 30,**

	2000	1999
Civil Service Retirement System	\$ 250	\$ 270
Federal Employees Health Benefits	446	445
Federal Employees Group Life Insurance	1	1
<b>Total Imputed Expenses-Employee Benefits</b>	<b>\$ 697</b>	<b>\$ 716</b>

**VETERANS BENEFITS**

Certain veterans who die or are disabled from military service-connected causes as well as their dependents receive compensation benefits and are provided with burial flags, headstones/markers, and grave liners for burial in a VA national cemetery or are provided a plot allowance for burial in a private cemetery. These benefits are provided in exchange for a veteran's military service and are recorded as a liability on the balance sheet.

**FEDERAL EMPLOYEE AND VETERANS BENEFITS LIABILITIES  
AS OF SEPTEMBER 30,**

	2000	1999
FECA	\$ 1,585	\$ 1,220
Compensation	542,900	480,300
Burial	2,800	2,900
<b>Total Federal Employee and Veterans Benefits Liabilities</b>	<b>\$ 547,285</b>	<b>\$ 484,420</b>

VA provides certain veterans and/or their dependents with pension benefits, based on annual eligibility reviews, if the veteran died or was disabled from non-service connected causes. The actuarial present value of the future liability for pension benefits is a non-exchange transaction and is not required to be recorded on the balance sheet. The projected liability for pension benefits (presented for informational purposes only) as of September 30, 2000, and 1999 was \$71.6 and \$73.3 billion, respectively.

**ASSUMPTIONS USED TO CALCULATE THE VETERANS BENEFITS LIABILITY**

Several significant actuarial assumptions were used in the valuation of compensation, pension, and burial benefits to calculate the present value of the liability. Future cash flows were discounted in perpetuity. A liability was recognized for the projected benefit payments to: (1) those beneficiaries, including veterans and survivors, currently receiving benefit payments; (2) current veterans who will in the future become beneficiaries of the compensation and pension programs; and (3) a proportional share of those in active military service as of the valuation date who will become veterans in the future. Survivors of those veterans in classes (1), (2), and (3) who receive benefits after death of the veteran are also incorporated into the projection.

Discount rates were based on rates on securities issued by the Treasury on September 30, 2000, ranging from 5.88 to 6.07 percent, and on September 30, 1999, ranging from 5.22 to 6.06 percent. Cash flows were assumed to occur at the midpoint of the fiscal year.

All calculations were done by program. The calculation for pension benefits was performed separately for each law: Protected (Old Law), Section 306, and P.L. 95-588. Burial liabilities were calculated on an overall basis.

Dollars by category and by age were used in the liability for compensation and pension benefits. Therefore, ratios, trends in caseloads, and mortality tables, were used to allocate dollars in these areas.

Life expectancies of veterans collecting benefits from the compensation and pension programs are based upon studies of mortality experience of those beneficiaries between 1994 and 2000. Life expectancies of veterans not collecting these benefits used in the calculation of the liability for future beneficiaries are based on mortality derived from the 1989-91 U.S. decennial census. Applying mortality improvements at a rate of 1 percent per annum brought both sets of mortality rates forward.

Cost of living adjustments (COLAs) were applied to determine the average benefits per veteran for each future time period. COLAs of 3.5 and 2.4 percent were assumed for fiscal years 2000 and 1999, respectively. For fiscal years after 2000, COLAs have been determined from OMB's estimates prepared in conjunction with the Administration's annual budget.

Expected benefit payments have been explicitly modeled for the next 70 years. This period is roughly the same as that used by the Office of the Actuary of the Social Security Administration (75 years). However, unlike Social Security, estimates of expected benefit payments after this 70-year period were reflected in the liability based on extrapolations reflecting aggregate experience by beneficiary category between the years 65 and 70.



## 14. INSURANCE PROGRAMS

The United States Government, through VA, administers five life insurance programs and the Veterans' Mortgage Life Insurance program for certain totally disabled veterans. VA supervises the Service Members' Group Life Insurance (SGLI) and the Veterans' Group Life Insurance (VGLI) programs, which provide life insurance coverage to members of the uniformed armed services, reservists, and post-Vietnam veterans. United States Code, Title 38, requires the Life Insurance programs to invest in Treasury securities.

### ADMINISTERED PROGRAMS

The United States Government Life Insurance (USGLI) program was the Government's first venture into life insurance. During WWI, the U.S. provided Marine Insurance to protect the interests of ship owners and merchants who were providing supplies to the allies in Europe. USGLI was the natural outgrowth of this Marine Insurance. The program was established to meet the needs of World War I veterans, but remained open to service members and veterans with service before October 8, 1940. The Government became a self-insurer since private insurance companies were unwilling to assume the unpredictable risks associated with a war. By establishing this program, Congress intended to avoid the financial burden imposed on the Government by the pension programs that were established after previous wars. The Government became the largest life insurer in the U.S. with the coverage provided by this program.

The National Service Life Insurance (NSLI) program covers policyholders who served during World War II. The program opened October 8, 1940, when it became clear that large-scale military inductions were imminent. Over 22 million policies were issued under the NSLI program. The majority of policies VA administers directly are NSLI policies. This program remained open until April 25, 1951, when two new programs were established for Korean War service members and veterans.

The Veterans' Special Life Insurance (VSLI) program was established in 1951 to meet the insurance needs of veterans who served during the Korean Conflict, and the post Korean period through January 1, 1957. During this period, all service members on active duty were covered for \$10,000, at no cost, under a program known as Servicemen's Indemnity. They remained covered for 120 days after their discharge. The VSLI program allowed these newly discharged service members to apply for \$10,000 of contract term insurance. Application had to be made during the 120-day period during which they remained covered by Servicemen's Indemnity. It was during this period that representatives of the commercial insurance industry began a major lobbying effort to get the Government out of the insurance business because the programs were viewed as competition. As a result, the VSLI program was closed to new issues at the end of 1956, and coverage for individuals in the services was terminated. Approximately 800,000 VSLI policies were issued between 1951 and 1957.

In addition to VSLI coverage, which was provided to healthy veterans, the Insurance Act of 1951 also established the Service-Disabled Veterans Insurance (S-DVI) program for veterans with service-connected disabilities. S-DVI is open to veterans separated from the service on or after April 25, 1951, who receive a service-connected



disability rating of 0 percent or greater. New policies are still being issued under this program.

In 1964, Congress enacted legislation providing for a limited reopening of NSLI and VSLI, and the Veterans' Reopened Insurance (VRI) program was established. Beginning May 1, 1965, veterans who had been eligible to obtain insurance between October 8, 1940 and January 1, 1957, could once again apply for government life insurance. They had one year to apply for this "reopened" insurance, which was available *only* to disabled veterans. Approximately 228,000 VRI policies were issued. No term insurance policies were issued in this program.

The Veterans' Mortgage Life Insurance (VMLI) program began in 1971, and is designed to provide financial protection to cover eligible veterans' home mortgages in the event of death. VMLI is issued to those severely disabled veterans who have received grants for Specially Adapted Housing from VA. These grants are issued to veterans whose movement is substantially impaired because of their disability. The maximum amount of VMLI allowed an eligible veteran is \$90,000. The insurance is payable if the veteran dies before the mortgage is paid off and is payable only to the mortgage lender.

#### **SUPERVISED INSURANCE PROGRAMS**

The Service Members' Group Life Insurance (SGLI) program was established in 1965, for Vietnam Era service members. SGLI is supervised by VA and is administered by the Office of Service Members' Group Life Insurance (OSGLI) under terms of a group insurance contract. This program provides low-cost term insurance protection to service members.

In 1974, the Veterans' Group Life Insurance (VGLI) program became available. VGLI, like SGLI, is supervised by VA, but is administered by the OSGLI. VGLI provides for the conversion of SGLI coverage to a five-year renewable term policy of insurance protection after a service member's separation from service.

#### **PUBLIC INSURANCE CARRIERS**

VA supervises the administration of the SGLI and VGLI programs. The Prudential Insurance Company of America (Prudential) provides veteran insurance coverage directly for the SGLI and VGLI programs. VA has entered into a Group Policy with the Prudential whereby Prudential and its reinsurers provide service members and veterans coverage in multiples of \$10,000 up to a maximum of \$200,000. The basic SGLI coverage is provided to those members on active duty in the Army, Navy, Air Force, Marine Corps, Coast Guard, commissioned members of the Public Health Service and the National Oceanic and Atmospheric Administration. The Ready Reserve is also insured by SGLI, and includes reservists and members of the National Guard who are assigned to a unit or position in which they may be required to perform active duty or active duty for training. The VGLI coverage is comprised of separated and retired active duty members and reservists who were covered under the Basic SGLI coverage.

Premiums for the SGLI and VGLI programs are set by mutual agreement between VA and Prudential. SGLI premiums for active duty personnel are deducted from their pay by the Armed Services components through the Department of Defense (DoD). DoD, through the Defense Finance and Accounting Service (DFAS), remits premiums collected to VA. The premiums are passed through to Prudential. Prudential records the premiums and maintains investments on their accounting record separate and independent from the VA reporting entity. VA monitors Prudential's insurance reserve balances to determine their adequacy and may increase or decrease the amounts retained by Prudential for contingency purposes. The reserves for the contingent liabilities are recorded in Prudential's accounting records and are not reflected in the VA reporting entity since the risk of loss on these programs is assumed by Prudential through the terms and conditions of the Group Policy.

Effective January 1, 1970, the Secretary of Veterans Affairs determines the costs that are traceable to the extra hazards of duty in the uniformed services, on the basis of the excess mortality incurred by members and former members of the uniformed armed services insured under SGLI, above what their mortality would have been under peacetime conditions. The Secretary is authorized to make adjustments regarding contributions from pay appropriations as may be indicated from actual experience.

### RESERVE LIABILITIES

The insurance reserves for administered programs are reported as liabilities covered by budgetary resources, while part of the S-DVI and VI&I reserves are reported as liabilities not covered by budgetary resources. Reserves for SGLI and VGLI are maintained in Prudential's financial records since the risk of loss is assumed by Prudential. Actuarial reserve liabilities for the administered life insurance programs are based on the mortality and interest assumptions at time of issue. These assumptions vary by fund, type of policy and type of benefit. The interest assumptions range from 2.25 to 5.0 percent. The mortality assumptions include the American Experience Table, the 1941 Commissioners Standard Ordinary (CSO) Table, 1958 CSO Basic Table, and the 1980 CSO Basic Table.

### INSURANCE LIABILITY (RESERVE) BALANCES

<b>INSURANCE LIABILITY RESERVE BALANCES AS OF SEPTEMBER 30,</b>	<b>Insurance Death Benefits</b>	<b>Death Benefit Annuities</b>	<b>Disability Income &amp; Waiver</b>	<b>Reserve Totals 2000</b>	<b>Reserve Totals 1999</b>
<b>Program</b>					
NSLI	\$ 10,196	\$ 238	\$ 248	\$ 10,682	\$ 10,821
USGLI	47	7	-	54	61
VSLI	1,395	14	43	1,452	1,421
S-DVI	413	2	114	529	524
VRl	435	3	7	445	456
VI&I	93	-	-	93	93
Subtotal	\$ 12,579	\$ 264	\$ 412	\$ 13,255	\$ 13,376
Less Liability not Covered by Budgetary Resources				(531)	(524)
<b>Liability Covered by Budgetary Resources</b>				<b>\$ 12,724</b>	<b>\$ 12,852</b>

### INSURANCE IN-FORCE

The amount of insurance in-force is the total face amount of life insurance coverage provided by each administered and supervised program as of the end of the fiscal year. It includes any paid-up additional coverage provided under these policies. Prudential and its reinsurers provided coverage to 2,720,085 and 2,692,160 insured for a face value of \$464.6 billion and \$461.9 billion as of September 30, 2000, and 1999, respectively. The face value of the insurance provided by Prudential and its reinsurers represents 95.5 and 95.3 percent of the total insurance in-force as of September 30, 2000, and 1999, respectively. The number of policies represents the number of active policies remaining in the program as of the end of each fiscal year.

<b>INSURANCE IN FORCE AS OF SEPTEMBER 30,</b>	<b>Policies 2000</b>	<b>Policies 1999</b>	<b>Face Value 2000</b>	<b>Face Value 1999</b>
<b>Supervised Programs</b>				
SGLI Active Duty	1,445,000	1,431,000	\$ 272,455	\$ 271,107
SGLI Ready Reservists	786,500	792,500	137,235	139,483
SGLI Post Separation	107,000	105,000	19,634	19,392
VGLI	381,585	363,660	35,259	31,899
<b>Total Supervised</b>	<b>2,720,085</b>	<b>2,692,160</b>	<b>464,583</b>	<b>461,881</b>
<b>Administered Programs</b>				
NSLI*	1,715,536	1,821,665	17,013	17,662
VSLI*	242,608	248,915	2,669	2,699
S-DVI	151,315	154,410	1,418	1,440
VRI*	77,638	82,617	648	675
USGLI	16,280	17,973	53	59
VMLI	3,457	3,518	198	201
<b>Total Administered</b>	<b>2,206,834</b>	<b>2,329,098</b>	<b>21,999</b>	<b>22,736</b>
<b>Total Supervised and Administered Programs</b>	<b>4,926,919</b>	<b>5,021,258</b>	<b>\$ 486,582</b>	<b>\$ 484,617</b>

\*1999 Policy counts were restated to include policies with only paid-up additional coverage.

### POLICY DIVIDENDS

The Secretary of VA determines annually the excess funds available for dividend payment. Dividends are based on an actuarial analysis of the individual programs at the end of the preceding calendar year. Dividends are declared on a calendar year basis and paid on policy anniversary dates. Policyholders can elect to: (1) receive a cash payment; (2) prepay premiums; (3) repay loans; (4) purchase paid-up insurance or (5) deposit the amount in an interest bearing account. A provision for dividends is charged to operations, and an insurance dividend is established when gains to operations are realized in excess of those essential to maintain solvency of the insurance programs. Policy dividends for fiscal years 2000 and 1999 were \$693 and \$755 million, respectively.

## 15. UNEXPENDED APPROPRIATIONS

The total unexpended balance is the sum of undelivered orders and unobligated balances. Appropriation acts and other provisions of law provide authority to incur new obligations. An obligation represents an amount that is expected to be expended upon

subsequent receipt of goods or services. The obligated balance is the cumulative amount of obligations incurred by VA for which outlays have not been made.

Undelivered orders are the amount of goods and services ordered for which delivery or performances have not yet occurred and are included in this balance. An unobligated balance is the amount available after deducting the cumulative obligations from total budgetary resources. In some instances, unobligated balances are not available due to legal constraints regarding the time limit and purpose for which funds can be obligated.

**UNEXPENDED APPROPRIATIONS  
AS OF SEPTEMBER 30,**

	2000	1999
<b>Unobligated Appropriations</b>		
Available	\$ 2,191	\$ 2,603
Unavailable	443	400
<b>Undelivered Orders</b>		
Paid	119	200
Unpaid	1,406	1,545
Other	(27)	-
<b>Total Unexpended Appropriations</b>	<u>\$ 4,132</u>	<u>\$ 4,748</u>

## 16. CONTINGENCIES

VA is a party in various administrative proceedings, legal actions, and tort claims arising from various sources including: disputes with contractors, challenges to compensation and education award decisions, loan guaranty indemnity debt cases, and allegations of medical malpractice. Certain legal matters to which VA may be a named party are administered and, in some instances, litigated by the Department of Justice. Generally, amounts (more than \$2,500 for Federal Tort Claims Act cases) to be paid under any decision, settlement, or award are funded from the Judgment Fund, which is maintained by Treasury. Of the amounts paid from the Judgment Fund, malpractice cases claimed 82 percent in FY 2000 and 80 percent in FY 1999. Contract dispute payments for FY 2000 and FY 1999 were \$4.8 and \$7.4 million, respectively.

VA has recorded a liability for pending legal claims that are estimated to be paid by the Judgment Fund. This liability is established for all pending claims whether reimbursement is required or not. This liability was \$415 million for FY 2000 and \$82 million for FY 1999. The significant increase in the liability for FY 2000 resulted from a change in the methodology used for the calculation. Additionally, there were 34 contract and personnel law cases totaling \$308.7 million where there was at least a reasonable possibility that a loss may occur. However, due to the unique fact and law considerations of each case and the statistically insignificant number of such cases, no estimate of liability could be made. VA is also required to record an operating expense and imputed financing source for the Judgment Fund's pending claims and

settlements. Judgment Fund accounting is shown below:

**JUDGMENT FUND**  
**AS OF SEPTEMBER 30,**

	2000	1999
Fiscal Year Settlement Payments	\$ 84	\$ 77
Less Contract Dispute Payments	(5)	(7)
Imputed Financing-Paid by Other Entities	79	70
Increase (Decrease) in Liability for Claims	70	13
<b>Operating Expense</b>	<b>\$ 149</b>	<b>\$ 83</b>

It is the opinion of VA's management and Office of General Counsel that resolution of pending legal actions as of September 30, 2000 will not materially affect VA's operations or financial position when consideration is given to the availability of the Judgment Fund appropriation to pay some court-settled legal cases. Fiscal year 2000 settlement payments were \$83.5 million.

The amount of unobligated and obligated authority relating to appropriations cancelled on September 30, 2000 and 1999, was \$101.2 million and \$102.5 million, respectively. Any payments that may arise relating to cancelled appropriations will be paid out of the current year's appropriations in accordance with the provisions of the Expired Funds Control Act of 1990.

## 17. ENVIRONMENTAL AND DISPOSAL

The Department of Veterans Affairs had unfunded environmental and disposal liabilities in the amount of \$240 million and \$199 million for the years ending September 30, 2000 and 1999, respectively. The majority of the unfunded liabilities involve asbestos removal, lead abatement, replacement of underground oil and gasoline tanks, decommissioning of waste incinerators, and decontamination of equipment prior to disposal.

While some facilities have applied prevailing state regulations that are more stringent than Federal guidelines, Occupational Safety and Health Administration (OSHA) and Environmental Protection Agency (EPA) are the legal basis for regulations behind the majority of VA's environmental and disposal liabilities. Estimated liabilities for these projects have been computed by the facility engineering staff based on similar projects already completed, or by independent contractors providing work estimates.

## 18. DISCLOSURES RELATED TO THE STATEMENTS OF BUDGETARY RESOURCES

### UNDELIVERED ORDERS

VA has obligations remaining at the end of each year for goods and services ordered but not yet received (undelivered orders). Aggregated undelivered orders amounted to \$1.7 billion and \$1.9 billion as of September 30, 2000 and 1999, respectively.

**BORROWING AUTHORITY**

Loan Guaranty had borrowing authority of \$1.2 billion and \$2 billion as of September 30, 2000, and 1999, respectively. The Vocational Rehabilitation Program had borrowing authority of \$2.5 and \$2.3 million as of September 30, 2000 and 1999, for making direct loans. Loan Guaranty borrowing was repaid to Treasury through the proceeds of portfolio loan collections, funding fees, and the sale of loans to Vinnie MAC trusts. The Vocational Rehabilitation loans generally had duration of 1 year, and repayment was made from offsetting collections.

**ADJUSTMENTS TO BUDGETARY RESOURCES**

Adjustment during the reporting period to budgetary resources available at the beginning of the year included VA appropriations that were subjected to a rescission of \$79.5 million taken from the multi-year medical care account.

**PERMANENT INDEFINITE APPROPRIATIONS**

VA has three permanent and indefinite appropriations. The Veterans Housing Benefit Program Fund (36X1119) covers all estimated subsidy costs arising from post-1991 loan obligations for Veterans Housing Benefits. The Fund's objective is to encourage and facilitate the extension of favorable credit terms by private lenders to veterans for the purchase, construction, or improvement of homes to be occupied by veterans and their families. The Loan Guarantee Revolving Fund (36X4025) is a liquidating account, which contains all of VA's pre-credit reform direct and guaranteed loans. It also holds fund balances received from reimbursements from financing accounts for loan modifications and rentals of foreclosed properties not yet transferred to financing accounts. This account is responsible for property management expenses prior to the sales of foreclosed properties. The Native American Direct Loan Account (36X1120) was established to cover all subsidy costs arising from direct loan obligations related to a veteran's purchase, construction, or renovation of a dwelling on trust land.

**USE OF UNOBLIGATED BALANCES OF BUDGET AUTHORITY**

Available unobligated balances on the Statement of Budgetary Resources are composed of current fiscal year apportioned funds for annual, multi-year, and no-year appropriations from Congress as well as revolving and trust funds. Other balances not available are composed of expired appropriation unobligated amounts, which generally are not available for new obligations, but can be used to increase existing obligations under certain circumstances. This amount also includes unobligated funds that were not apportioned by OMB for FY 2000 use.

Unobligated VA funds are available for uses defined in VA's FY 2000 Appropriation Law (P.L. 106-74). These purposes include: veterans' medical care, research, education, construction and maintenance of VA buildings, veterans' and dependents' benefits, veterans' life insurance, loan guaranty programs, veterans' burial benefits, and administrative functions. Various obligation limitations are imposed on individual VA appropriations. Examples include travel obligation limitations and limitation of the use of medical care multi-year funds to object classes for equipment, structures, and land.



## CONTRIBUTED CAPITAL

The amount of contributed capital received during the fiscal year consisted of donations in the amount of \$45 million to the General Post Fund and \$0.2 million to the National Cemetery Gift Fund.

## 19. EXCHANGE TRANSACTIONS

### EXCHANGE REVENUES

Exchange revenues normally require reporting entities to recover full cost. The Veterans Health Administration (VHA) has legislated exceptions to the requirement that user charges be sufficient to recover the full cost to the Federal Government of providing the service, resource, or good. Under “enhanced sharing authority”, arrangements entered into shall provide for payment to the Department in accordance with procedures that provide appropriate flexibility to negotiate payment, which is in the best interest of the Federal Government.

VA’s Loan Guaranty Line of Business collects rental fees on a small number of properties during the period when the property is titled to the VA. The National Cemetery Administration (NCA) leases lodges at 16 cemeteries to Not-for-Profit groups for no fee. The Not-for-Profit groups are required to provide the upkeep on the lodges and pay the costs for utilities, insurance, minor repairs and maintenance and any other costs associated with the lodges. NCA paid \$53 thousand to perform repairs at the City Point, Cold Harbor, Culpeper, Glendale, Jefferson City, Richmond, Saint Augustine, Seven Pines, and Winchester National Cemetery lodges.

NCA also has three agricultural leases with private companies/individuals. Fort Snelling National Cemetery received no fees but received 7,000 cubic yards of clean wood chips and 14,000 cubic yards of clean compost for the use of developed cemetery land for lease of land to a mulching facility. The estimated value of the wood chips and compost is \$287 thousand. Administrative/contracting support was provided to the cemetery by the Contracting Officer of the VAMC Minneapolis, MN and administrative/legal support was provided by the Office of Regional Counsel, Minneapolis, MN. The lessee is required to pay all costs of maintaining the facility. Houston National Cemetery leases 251 acres of undeveloped land for \$9 thousand for grazing and cultivation of grass or hay for livestock purposes. The lessee is required to pay all costs. Saratoga Springs National Cemetery has land leased by a sod farmer and received sod that has an estimated value of \$1 thousand. The VAMC Albany District Counsel provided administrative support. In addition, the NCA received fees for filming performed at one cemetery. The Los Angeles National Cemetery received \$4 thousand for filming and had costs of \$3 hundred for the Director’s Services.

### EXCHANGE TRANSACTIONS WITH PUBLIC

Exchange transactions with the public occur when prices are set by law or executive order and are not based on full cost or on market price. VA’s Medical Care Collections Fund, “Conforming Amendments,” changed the language of specific sections of 38 USC Chapter 17 to substitute “reasonable charges” for “reasonable cost.” The VHA Chief Financial Officer (CFO) is responsible for implementing and maintaining these reasonable charges for billing third party payers for services provided to insured veterans for treatment of nonservice-connected conditions.

Reasonable charges are used to bill for reimbursable health insurance, non-Federal workers' compensation and no-fault or uninsured motorists insurance cases. Reasonable charges are based on provider charges in the market area of each VA facility. The lesser of VA billed charges or their usual customary and reasonable payment to other providers will be paid. Cost-based per diems are calculated annually to produce Tort Rates used to bill for tortfeasor, workers' compensation (other than Federal), humanitarian emergencies, ineligibles, VA employee, family member, allied beneficiary, no fault or uninsured motorist's insurance, or reimbursable insurance cases. These per diem costs are derived primarily from cost and workload data from a national cost allocation report (Cost Distribution Report).

Fees to be charged by VA for requests for information under the Freedom of Information Act (FOIA) are governed by 38 CFR Section 1.555. There are four categories of FOIA requesters: (1) commercial use; (2) educational and non-commercial scientific institutional; (3) representatives of the news media; and (4) all other. Specific levels of fees are to be charged for each of the categories. Categories (2), (3) and (4) are entitled to receive 100 pages of reproduced material and the first two hours of search time without charge. Commercial use requesters are to be charged the full direct costs of searching for, reviewing for release, and duplicating the records sought. Direct costs include the salary of the employee performing the work and the cost of operating duplicating machinery, but do not include overhead expenses such as costs of space, and heating or lighting of the facility in which the records are stored. Under certain circumstances, fees can be waived or reduced at the discretion of field facility heads, their designee, or responsible Central Office officials.

VA is required to collect a co-payment of \$2 from veterans for treatment of a nonservice-connected condition for each 30-day supply of medication furnished on an outpatient basis. This fee does not cover the cost of the medications in the vast majority of cases.

VA's Loan Guaranty Line of Business collects certain fees that are set by law. The loan guarantee funding fees collected for fiscal year 2000 were \$421.1 million. The loan guarantee lender participation fees collected for fiscal year 2000 were \$2.1 million.

### **INTRAGOVERNMENTAL EXCHANGE TRANSACTIONS**

This section discloses intragovernmental exchange transactions in which VA provides goods or services at a price less than the full cost or does not charge a price at all with explanations for disparities between the billing and full cost.

VA and DoD have authority to enter into agreements and contracts for the mutual use or exchange of use of hospital and domiciliary facilities and other resources. The providing agency shall be reimbursed for the cost of the health-care resources based on the methodology agreed to by VA and DoD. Facility Directors have the flexibility to consider local conditions and needs and the actual costs of providing the services. VA's General Counsel has determined that full cost recovery is not mandated, VHA captures the total amount of reimbursements received under DoD sharing agreements but the total amount billed below full cost is not readily available. VHA is in the process of developing mechanisms to report this information in the future. The Benefits Line of



Business collects funding from DoD in order to administer certain education programs. DoD transferred \$213 million during the year for the Post-Vietnam Era Education Assistance Program (VEAP), Reinstated Entitlements Program for Survivors (REPS) and the New GI Bill for Veterans.

When VA furnishes medical care or services for beneficiaries of other Federal agencies, and that care or service is not covered by an applicable local sharing agreement, the billing rates used are determined and published annually by the VHA CFO. Similar to the Tort Rates, interagency billing rates are determined from cost and workload data in the Cost Distribution Report.

### SCHEDULE OF NET PROGRAM COST

AS OF  
SEPTEMBER 30,  
2000  
(DOLLARS IN  
MILLIONS)

	MEDICAL CARE	MEDICAL EDUCATION	MEDICAL RESEARCH	COMPENSATION	PENSION	EDUCATION	VOCATIONAL REHAB	LOAN GUARANTY	INSURANCE	BURIAL	OTHER	TOTAL
<b>PRODUCTION COSTS</b>												
<b>Governmental Costs</b>	\$ 3,153	\$ 113	\$ 101	\$ 167	\$ 60	\$ 34	\$ 30	\$ 53	\$ 16	\$ 26	\$ 30	\$ 3,783
<b>Less Earned Revenues</b>	(51)	-	(24)	-	(14)	(188)	-	(463)	(1,066)	-	(195)	(2,001)
<b>Net Governmental Production Costs</b>	3,102	113	77	167	46	(154)	30	(410)	(1,050)	26	(165)	1,782
<b>Public Costs</b>	17,211	669	644	82,017	3,115	1,341	466	109	1,884	127	173	107,756
<b>Less Earned Revenues</b>	(1,282)	-	(3)	-	-	(103)	-	(122)	(734)	-	(15)	(2,259)
<b>Net Public Production Costs</b>	15,929	669	641	82,017	3,115	1,238	466	(13)	1,150	127	158	105,497
<b>Non-Production Costs</b>												
<b>Hazardous Waste Clean-up</b>	41	-	-	-	-	-	-	-	-	-	-	41
<b>Net Program Costs</b>	19,072	782	718	82,184	3,161	1,084	496	(423)	100	153	(7)	107,320
<b>Net Non-VA Program Costs</b>	-	-	-	-	-	-	496	-	-	-	(10)	(10)
<b>Total Net Cost of Operations</b>	\$19,072	\$ 782	\$ 718	\$ 82,184	\$ 3,161	\$ 1,084	\$ 496	\$ (423)	\$ 100	\$ 153	\$ (17)	\$ 107,310

## SCHEDULE OF NET PROGRAM COST

AS OF  
SEPTEMBER 30,  
1999  
(DOLLARS IN  
MILLIONS)

	MEDICAL CARE	MEDICAL EDUCATION	MEDICAL RESEARCH	COMPENSATION	PENSION	EDUCATION	VOCATIONAL REHAB	LOAN GUARANTY	INSURANCE	BURIAL	OTHER	TOTAL
<b>PRODUCTION COSTS</b>												
<b>Governmental Costs</b>	\$ 1,332	\$ -	\$ 653	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 1,985
<b>Less Earned Revenues</b>	(72)	-	(39)	-	(17)	(188)	-	-	(1,113)	-	-	(1,429)
<b>Net Governmental Production Costs</b>	1,260	-	614	-	(17)	(188)	-	-	(1,113)	-	-	556
<b>Public Costs</b>	17,183	830	38	(75,607)	3,266	1,305	509	1,683	1,965	(599)	-	(49,427)
<b>Less Earned Revenues</b>	(928)	-	(2)	-	-	(173)	-	(432)	(781)	-	-	(2,316)
<b>Net Public Production Costs</b>	16,255	830	36	(75,607)	3,266	1,132	509	1,251	1,184	(599)	-	(51,743)
<b>Non-Production Costs</b>	-	-	-	-	-	-	-	-	-	-	-	-
<b>Hazardous Waste Clean-up</b>	58	-	-	-	-	-	-	-	-	1	-	59
<b>Net Program Costs</b>	17,573	830	650	(75,607)	3,249	944	509	1,251	71	(598)	-	(51,128)
<b>Net Non-VA Program Costs</b>	-	-	-	-	-	-	-	-	-	-	10	10
<b>Total Net Cost of Operations</b>	\$ 17,573	\$ 830	\$ 650	\$(75,607)	\$ 3,249	\$ 944	\$ 509	\$ 1,251	\$ 71	\$ (598)	\$ 10	\$(51,118)

## 20. DEDICATED COLLECTIONS

In the Federal Government, dedicated collections are accounted for in trust funds and special funds. The term "trust funds" as used in this report and in Federal budget accounting is frequently misunderstood. In the private sector, "trust" refers to funds of one party held by a second party (the trustee) in a fiduciary capacity. In the Federal budget, the term "trust fund" means only that the law requires that funds be accounted for separately, used only for specified purposes and that the account was designated as a "trust fund." A change in law may change the future receipts and the terms under which the fund's resources are spent. The "trust fund assets" represent all sources of receipts and amounts due the trust fund regardless of source. This includes "related governmental transactions," which are transactions between two different entities within the Federal Government. The "Investments with Treasury" assets are comprised of investments in Federal debt securities and related accrued interest. These securities will require redemption if a fund's disbursements exceed its receipts. Unless

specifically provided for by law, trust funds may only place excess funds in Federally backed investments (e.g., Federal debt securities).

The table below summarizes the name, type, and purpose of the funds within VA that receive dedicated collections. All of the funds listed use the accrual basis of accounting. However, collections are reported as actually received in accordance with OMB Circular A-34. The insurance funds listed also adhere to the requirements of FASB No. 120 "Accounting and Reporting by Mutual Life Insurance Enterprise", and issue a separate annual report. All of the funds generally receive authority to use current year contributions as well as a portion of previously contributed amounts.

FUND NAME	FUND TYPE	TREASURY SYMBOL	AUTHORITY	PURPOSE OF FUND	FINANCING SOURCES
<b>MEDICAL CARE COLLECTIONS FUND</b>	Special	36x5287	P.L. 105-33	Accumulates recoveries from third parties and patient co-payments.	Public, primarily insurance carriers.
<b>ESCROWED FUNDS FOR SHARED MEDICAL EQUIPMENT PURCHASES</b>	Deposit	36x6019	106 STAT. 1974	Receives payments from public companies involved in joint purchases of medical equipment.	Public, universities, pharmaceuticals & other medical organizations.
<b>PERSONAL FUNDS OF PATIENTS</b>	Deposit	36x6020	38 U.S.C. 3204	Temporarily holds funds.	Public, patients.
<b>EMPLOYEE ALLOTMENTS FOR SAVINGS BONDS</b>	Deposit	36x6050	31 U.S.C. 3105	Temporarily holds funds.	Employees.
<b>CEMETERY GIFT FUND</b>	Trust	36x8129	38 U.S.C. 1007	Expenditure of funds is limited to cemeteries by donor.	Public donors.
<b>NATIONAL SERVICE LIFE INSURANCE FUND</b>	Trust	36x8132	38 U.S.C. 720	Accumulates premiums to insure veterans of WWII.	Public, veterans.
<b>POST-VIETNAM ERA EDUCATION ASSISTANCE PROGRAM</b>	Trust	36x8133	38 U.S.C. 1622	To subsidize the cost of education to veterans.	Veterans, DoD.
<b>U.S. GOVERNMENT LIFE INSURANCE</b>	Trust	36x8150	38 U.S.C. 755	Premiums insure WWI veterans.	Public, veterans.
<b>VETERANS SPECIAL LIFE INSURANCE FUND</b>	Trust	36x8455	38 U.S.C. 723 101-228	Premiums insure Korean War Vets without Service-related disabilities.	Public, veterans.
<b>GENERAL POST FUND, NATIONAL HOMES</b>	Trust	36x8180	38 U.S.C. 101-228	Receives restricted and unrestricted use donations	Public, mostly veterans.

The following tables provide condensed information on assets, liabilities, fund balances, net costs, and changes in fund balances:

**AS OF SEPTEMBER 30, 2000****FUND SYMBOL****Assets:**

	5287	8129	8132	8133	8150	8455	8180	TOTAL
Fund balance with Treasury	\$ 59	\$ -	\$ 7	\$ 98	\$ -	\$ 1	\$ (2)	\$ 163
Investments with Treasury	-	-	12,019	-	75	1,745	59	13,898
Other Assets	724	3	728	1	3	117	20	1,596
<b>Total Assets</b>	783	3	12,754	99	78	1,863	77	15,657
<b>Liabilities:</b>								
Payables to Beneficiaries	-	-	123	1	2	8	1	135
Other Liabilities	-	-	12,257	-	73	1,777	2	14,109
<b>Total Liabilities</b>	-	-	12,380	1	75	1,785	3	14,244
<b>Net Position:</b>								
Cumulative Results	783	3	374	98	3	78	74	1,413
<b>Total Liabilities &amp; Net Position</b>	\$ 783	\$ 3	\$ 12,754	\$ 99	\$ 78	\$ 1,863	\$ 77	\$ 15,657

**FOR THE YEAR ENDED  
SEPTEMBER 30, 2000****FUND SYMBOL****Revenues:**

	5287	8129	8132	8133	8150	8455	8180	TOTAL
Exchange - Federal	\$ (12)	\$ -	\$ 879	\$ -	\$ 5	\$ 143	\$ -	\$ 1,015
Exchange - Public	943	-	600	4	-	77	1	1,625
Non-Exchange - Federal	-	-	-	-	-	-	3	3
Non-Exchange - Public	-	-	-	-	-	-	45	45
<b>Total Revenues</b>	931	-	1,479	4	5	220	49	2,688
<b>Expenses:</b>								
Program Expenses	25	-	1,527	15	5	224	44	1,840
<b>Total Expenses</b>	25	-	1,527	15	5	224	44	1,840
<b>Net Change from Operations</b>								
Beginning Net Position	441	3	420	108	4	81	78	1,135
Net Change from Operations	905	-	(48)	(11)	(1)	(4)	5	846
Non-Operating Changes	(564)	-	2	-	-	-	(8)	(570)
<b>Ending Equity</b>	\$ 782	\$ 3	\$ 374	\$ 97	\$ 3	\$ 77	\$ 75	\$ 1,411

## 21. DISCLOSURES RELATED TO THE STATEMENTS OF FINANCING

The total amount of VA liabilities not covered by budgetary resources was \$549.7 billion and \$486.4 billion as of September 30, 2000 and 1999, respectively. The following table contains the components of the balance sheet liability:

### COMPONENTS OF UNFUNDED LIABILITIES AS OF SEPTEMBER 30,

	2000	1999
Workers' Compensation*	\$ 1,906	\$ 1,533
Annual Leave	936	904
Judgment Fund	415	82
Environmental and Disposal	240	199
Capital Leases	8	1
Veterans Compensation and Burial	545,700	483,200
Insurance	531	524
<b>Total</b>	<b>\$ 549,736</b>	<b>\$ 486,443</b>

\* The actuarial estimate for workers' compensation provided by DOL was computed using interest rates of 6.15 to 6.3 percent for FY 2000 and 5.5 to 5.6 percent for FY 1999. The Statement of Financing line "total financing sources yet to be provided" only reflects the amount of increases/decreases in these liabilities. For existing liabilities, there will always be a difference between the "financing sources" line and the balance sheet amount.

## 22. RESTATEMENTS, RECLASSIFICATIONS AND CHANGES IN ACCOUNTING PRINCIPLES

### RECLASSIFICATIONS

On the 2000 and 1999 Statement of Net Cost, VA reclassified the change in veterans actuarial liability in order to not distort the program activity being reported in the compensation and burial activities. A new section on the Statement of Net Cost, titled "Changes in Veterans Benefits Actuarial Liabilities" reflects the costs. This change results in an increase of \$94,127 and \$822 million in the FY 1999 program cost lines for Compensation and Burial respectively.

### PRIOR PERIOD ADJUSTMENT

In FY 2000, the contingent liability for claims for medical malpractice increased due to changes in the method used to estimate the amount. Using an actuarial analysis, the estimate for future medical malpractice payments was revised to reflect out year payments including legal and other overhead costs. A prior period adjustment of \$263 and \$(3) million is reported on the Statement of Changes in Net Position for FY 2000 and 1999 respectively.

### CHANGES IN ACCOUNTING PRINCIPLES

The capitalization threshold for VA's fixed assets was raised from \$5,000 to \$25,000. The system modifications to account for this change were completed for real property during FY 1999 and for personal property during FY 2000. A line titled "Cumulative

Effect of Change in Accounting Principle” has been included on the Statement of Changes in Net Position to report the \$503 and \$60 million reduction in property, plant, and equipment book value for FY 2000 and 1999, respectively.

### 23. NON-ENTITY ASSETS AND LIABILITIES

Entity and Non-Entity assets and liabilities have been combined on the face of the balance sheet. Non-Entity assets and liabilities relate primarily to patient funds and funds for shared purchases of medical equipment. The Fund Balance with Treasury amount recorded as a Special Fund non-entity balance in FY 1999 has been returned to Treasury using a newly established Treasury General Fund Receipt Account. Fund Balance with Treasury amounts related to Credit Reform subsidy downward reestimates will no longer be retained in VA Special Funds.

#### NON-ENTITY ASSETS AS OF SEPTEMBER 30,

	2000	1999
Intragovernmental		
Fund Balance with Treasury	\$ 44	\$ 1,815
Accounts Receivable	-	1
Other	3	-
Public Accounts Receivable	-	6
<b>Total Non-Entity Assets</b>	<b>\$ 47</b>	<b>\$ 1,822</b>

#### Non-Entity Liabilities

Intragovernmental		
Other	-	1,772
Public		
Other	47	50
<b>Total Non-Entity Liabilities</b>	<b>\$ 47</b>	<b>\$ 1,822</b>

**REQUIRED SUPPLEMENTARY  
INFORMATION  
(UNAUDITED)**

**REQUIRED SUPPLEMENTARY STEWARDSHIP INFORMATION****HERITAGE ASSETS**

Heritage assets are property that possess one or more of the following characteristics; historical or natural significance; cultural; educational or aesthetic value; or significant architectural characteristics. The monetary value of heritage assets is often not estimable or relevant. By nature they are expected to be maintained in perpetuity. VA has medical centers and national cemeteries that meet the criteria for a heritage asset. During the reporting period, all maintenance expenses were recorded as incurred. Heritage assets are reported in terms of physical units.

**HERITAGE ASSETS IN UNITS****AS OF SEPTEMBER 30,**

	2000	1999
Art Collections	34	34
Buildings and Structures	1,883	1,878
Monuments/Historic Flag Poles	235	294
Other Non-Structure Items	54	19
Archaeological	11	-
Cemeteries	157	154
<b>Total Heritage Assets in Units</b>	<b>2,374</b>	<b>2,379</b>

**DEFERRED MAINTENANCE**

Deferred maintenance is classified as not performed when it should have been or scheduled and delayed to a future period. It is VA policy to assure that medical equipment and critical facility equipment systems are maintained and managed in a safe and effective manner; therefore, deferred maintenance is not applicable to them. VA facilities reported their cost estimates for deferred maintenance by utilizing either the Condition Assessment Survey or the Total Life-Cycle Cost Method.

**DEFERRED MAINTENANCE****YEARS ENDED SEPTEMBER 30,**

	2000	1999
General PP&E	\$ 1,043	\$ 835
Heritage Assets	28	24
<b>Total Deferred Maintenance</b>	<b>\$ 1,071</b>	<b>\$ 859</b>



### NON-FEDERAL PHYSICAL PROPERTY

The VA Extended Care Facilities Grant Program assists states in acquiring facilities for furnishing domiciliary or nursing home care to veterans, and to expand, remodel, or alter existing buildings for furnishing domiciliary, nursing home, or hospital care to veterans in state homes. Currently, these grants may not exceed 65 percent of the total project cost.

VA's State Cemetery Grants Program is authorized to pay up to 100 percent of the cost of constructing and equipping state veterans cemeteries. States provide the land and agree to operate the cemeteries. In FY 2000, new grants were awarded totaling more than \$62 million.

#### GRANT PROGRAM COSTS AS OF SEPTEMBER 30,

	2000	1999
State Extended Care Facilities	\$ 20	\$ 36
State Veterans Cemeteries	19	3
<b>Total Grant Program Costs</b>	<b>\$ 39</b>	<b>\$ 39</b>

### HUMAN CAPITAL

Investment in human capital comprises those expenses for education and training programs for the general public that are intended to increase or maintain national economic productive capacity. It does not include expenses for internal Federal education and training of civilian employees. Educational programs assist active duty and reservist veterans, eligible under the MGIB or the Veterans Educational Assistance Program (VEAP), as well as dependents of veterans who died of service-connected disabilities or whose service-connected disabilities were rated permanent and total. The Vocational Rehabilitation Program provides veterans, having a 10 percent or greater service-connected disability rating who are found to have a serious employment handicap, with evaluation services, counseling, and training necessary to assist them in becoming employable and maintaining employment to the extent possible.

**VETERANS AND DEPENDENTS EDUCATION  
AS OF SEPTEMBER 30,**

	2000	1999
<b>Program Expenses</b>		
Education and Training-Dependents of Veterans	\$ 138	\$ 136
Vocational Rehabilitation and Education Assistance	1,426	1,448
Administrative Program Costs	147	78
<b>Total Program Expenses</b>	<b>\$ 1,711</b>	<b>\$ 1,662</b>
<b>Program Outputs (Participants)</b>		
Dependent Education	44,820	44,423
Veterans Rehabilitation	52,786	52,284
Veterans Education	352,770	362,010

**HEALTH PROFESSIONS EDUCATION**

Title 38 U.S.C. mandates that VA assist in the training of health professionals for its own needs and for those of the Nation. By means of its partnerships with affiliated academic institutions, VA conducts the largest education and training effort for health professionals in the Nation. Each year, approximately 90,000 medical and other students receive some or all of their clinical training in VA facilities through affiliations with over 1,200 educational institutions including 107 medical schools. Many of these trainees have their health professional degrees and contribute substantially to VA's ability to deliver cost-effective and high-quality patient care during their advanced clinical training at VA.

**HEALTH PROFESSIONS EDUCATION****YEARS ENDED SEPTEMBER 30,**

	2000	1999
<b>Program Expenses</b>		
Physician Residents and Fellows	\$ 364	\$ 357
Associated Health Residents and Students	44	42
Instructional and Administrative Support	334	327
<b>Total Program Expenses</b>	<b>\$ 742</b>	<b>\$ 726</b>
<b>Program Outputs</b>		
Health Professions Rotating Through VA:		
Physician Residents and Fellows	28,921	31,012
Medical Students	17,706	18,771
Nursing Students	20,185	25,549
Associated Health Residents and Students	17,698	16,499
<b>Total Program Outcomes</b>	<b>84,510</b>	<b>91,831</b>

**PROGRAM EXPENSE  
AS OF SEPTEMBER 30,**

				2000	1999
	Basic	Applied	Development	Total	Total
Medical Research Service	\$ 158	\$ 50	\$ -	\$ 208	\$ 198
Rehabilitative Research and Development	3	15	9	27	28
Environmental Epidemiology Service	-	-	-	-	2
Health Services Research and Development	-	43	-	43	40
Cooperative Studies Research Service	-	42	-	42	42
Medical Research Support	-	340	-	340	321
Prosthetic Research Support	-	5	-	5	5
<b>Total Program Expenses</b>	<b>\$ 161</b>	<b>\$ 495</b>	<b>\$ 9</b>	<b>\$ 665</b>	<b>\$ 636</b>

**RESEARCH AND DEVELOPMENT**

Investments in research and development comprise those expenses for basic research, applied research, and development that are intended to increase or maintain national economic productive capacity or yield other benefits. For FY 2000, VA's R&D general goal related to stewardship was to ensure that VA medical research programs met the needs of the veteran population and contributed to the Nation's knowledge about disease and disability. Target levels were established for the: (1) percent of funded research projects relevant to VA's health-care mission in designated research areas and (2) number of research and development projects. Strategies were developed in order to ensure that performance targets would be achieved. In addition, VHA researchers received grants from National Institutes of Health (NIH) in the amount of \$244.8 million and \$175.3 million in other grants during FY 2000. These grants were given directly to the researchers and are not considered part of the VA entity. They are being disclosed here as Required Supplementary Stewardship Information but are not accounted for in the financial statements.

**RESEARCH AND DEVELOPMENT MEASURES-ACTUAL  
AS OF SEPTEMBER 30,**

	2000	1999
Percent of Funded Research Projects Relevant to VA's Health-Care Mission	99%	99%
Number of Research and Development Projects	1,942	2,013

## REQUIRED SUPPLEMENTARY INFORMATION

### SEGMENT INFORMATION

#### CONDENSED BALANCE SHEET

AS OF SEPTEMBER 30,

	SUPPLY FUND		ENTERPRISE FUND	
	2000	1999	2000	1999
<b>Assets</b>				
Fund Balance with Treasury	\$ 220	\$ 129	\$ 45	\$ 34
Accounts Receivable, Net	77	34	10	3
General Property, Plant and Equipment	6	8	14	10
Other Assets Including Inventory	25	34	2	-
<b>Total Assets</b>	<b>\$ 328</b>	<b>\$ 205</b>	<b>\$ 71</b>	<b>\$ 47</b>
<b>Liabilities and Net Position</b>				
Accounts Payable	\$ 131	\$ 64	\$ 2	\$ 11
Deferred Revenues	73	13	-	-
Other Liabilities	4	3	25	8
<b>Total Liabilities</b>	<b>208</b>	<b>80</b>	<b>28</b>	<b>19</b>
Cumulative Results of Operations	120	125	43	28
<b>Total Liabilities and Net Position</b>	<b>\$ 328</b>	<b>\$ 205</b>	<b>\$ 71</b>	<b>\$ 47</b>
<b>Condensed Net Cost Information</b>				
<b>Total Program Costs</b>	<b>\$ 622</b>	<b>\$ 548</b>	<b>\$ 124</b>	<b>\$ 93</b>
<b>Earned Revenues</b>				
Intra-Departmental	(413)	(437)	(132)	(89)
Other Federal Entities	(183)	(82)	(6)	(6)
Non-Federal	(23)	(19)	-	-
<b>Total Earned Revenues</b>	<b>(619)</b>	<b>(538)</b>	<b>(138)</b>	<b>(95)</b>
<b>Net Program Costs</b>	<b>\$ 3</b>	<b>\$ 10</b>	<b>\$ (14)</b>	<b>\$ (2)</b>

#### ENTERPRISE FUND SERVICES

The Enterprise Fund is the entrepreneurial organization of the VA Franchise Fund authorized under GMRA and which provides a wide range of services to both VA and the other Federal agencies, including DoD, Housing and Urban Development, and General Accounting Office. The Fund consists of six Enterprise Centers: The Financial Services Center (FSC) processes and or provides payments, purchase card transactions and travel vouchers, electronic data interchange and accounting support. The Austin Automation Center (AAC) supports general application and other systems which include: payroll, financial management, vendor payment, logistics, centralized medical systems and integrated patient care databases, benefits delivery applications, time sharing, communications with VA and non-VA entities, local and wide area network management and office automation support.

The VA Records Center and Vault provides services including secure archival storage and protection and retrieval services for veterans' and other Federal records. The VA Law Enforcement Training Center, available to the approximately 2,400 law enforcement personnel working at VA health-care facilities and to Federal law enforcement professionals at other government agencies, provides special training for police officers who work in health-care or service-oriented environments. The Security and Investigations Center provides quality and timely investigations and adjudication for employees in sensitive and or public trust positions. The Debt Management Center provides direct collection of delinquent consumer debt owed to VA.

### SUPPLY FUND SERVICES

The Supply Fund functions include stocking, repairing, and distributing supplies, medical equipment, and devices; providing forms, publications, and a full range of printing and reproduction services; training VA medical acquisition, supply, processing, and distribution personnel; and increasing small and disadvantaged business participation in VA contracts. The primary customer for the Supply Fund is VA, but the Fund also has significant sales to other Federal agencies including DoD and Health and Human Services.

### BALANCES WITH OTHER FEDERAL ENTITIES

#### INTRAGOVERNMENTAL ASSETS

AS OF SEPTEMBER 30, 2000

	Fund Balance with Treasury	Investments	Accounts Receivable	Other Assets
<b>Trading Partners</b>				
Treasury	\$ 12,434	\$ 14,450	\$ 171	\$ -
GSA	-	-	-	33
All Other	-	-	88	60
<b>Total Intragovernmental Assets</b>	<b>\$ 12,434</b>	<b>\$ 14,450</b>	<b>\$ 259</b>	<b>\$ 93</b>

#### INTRAGOVERNMENTAL LIABILITIES

AS OF SEPTEMBER 20, 2000

	Accounts Payable	Debt	Other
<b>Trading Partners</b>			
Treasury	\$ -	\$ 1,827	\$ 2,253
Other	37	-	197
<b>Total Intragovernmental Liabilities</b>	<b>\$ 37</b>	<b>\$ 1,827</b>	<b>\$ 2,450</b>

**INTRAGOVERNMENTAL EARNED REVENUES AND RELATED COSTS**  
**YEAR ENDED SEPTEMBER 30, 2000**

<b>Trading Partners</b>		<b>Earned Revenue</b>	
Treasury		\$	1,556
All Other			465
<b>Total Federal Earned Revenue</b>		\$	2,021
<b>Budget Functional Classification</b>		<b>Gross Cost to Generate Revenue</b>	
Veterans Benefits and Services		\$	1,991

**INTRAGOVERNMENTAL NON-EXCHANGE REVENUE**  
**YEAR ENDED SEPTEMBER 30, 2000**

<b>Trading Partner</b>		<b>Transfers-In</b>		<b>Transfers-Out</b>
Treasury	\$	-	\$	1,083

## SCHEDULE OF BUDGETARY ACTIVITY

				SPENDING AUTHORITY			
	TOTAL OUTLAYS	BUDGETARY RESOURCES	OBLIGATIONS INCURRED	FROM OFFSETTING COLLECTIONS AND ADJUSTMENTS	OBLIGATED BALANCE OCT. 1, 2000	OBLIGATED BALANCE SEPT. 30, 2000	
<b>VHA</b>							
0160 Medical Care	\$ 19,249	\$ 20,927	\$ 19,237	\$ 112	\$ 2,572	\$ 2,448	
0161 Medical & Prosthetic Research	329	389	349	27	110	102	
All Other	539	1,491	734	270	703	628	
<b>Total</b>	<b>\$ 20,118</b>	<b>\$ 22,808</b>	<b>\$ 20,320</b>	<b>\$ 409</b>	<b>\$ 3,385</b>	<b>\$ 3,178</b>	
<b>VBA</b>							
0102 Compensation, Pension, & Burial Benefits	\$ 23,820	\$ 22,337	\$ 22,166	\$ -	\$ 1,697	\$ 43	
0137 Readjustment Benefits	1,497	1,693	1,667	191	58	37	
4025 Housing Credit Liquidating	(255)	585	341	554	45	88	
4127 Direct Loan Financing	(70)	2,039	1,761	1,820	(1)	9	
4129 Guaranteed Loan Financing	(673)	8,010	3,168	3,896	77	22	
8132 National Service Life Insurance Fund	1,242	12,159	1,733	497	1,390	1,385	
All Other	1,775	6,535	4,128	2,419	396	329	
<b>Total</b>	<b>\$ 27,337</b>	<b>\$ 53,354</b>	<b>\$ 34,963</b>	<b>\$ 9,377</b>	<b>\$ 3,664</b>	<b>\$ 1,913</b>	
<b>NCA</b>							
0129 National Cemetery System	\$ 95	\$ 98	\$ 96	\$ -	\$ 15	\$ 16	
All Other	12	35	19	-	15	22	
<b>Total</b>	<b>\$ 108</b>	<b>\$ 133</b>	<b>\$ 115</b>	<b>\$ -</b>	<b>\$ 31</b>	<b>\$ 38</b>	
<b>ADM</b>							
0151 General Operating Expenses	\$ 881	\$ 1,241	\$ 1,218	\$ 289	\$ 142	\$ 190	
All Other	(64)	1,034	838	821	1	83	
<b>Total</b>	<b>\$ 817</b>	<b>\$ 2,274</b>	<b>\$ 2,056</b>	<b>\$ 1,109</b>	<b>\$ 143</b>	<b>\$ 272</b>	
<b>Total of all Business Lines</b>	<b>\$ 48,380</b>	<b>\$ 78,569</b>	<b>\$ 57,455</b>	<b>\$ 10,895</b>	<b>\$ 7,222</b>	<b>\$ 5,402</b>	

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